(19) No. 97-1732-CFX Title: California Public Employees' Retirement System, et al., Petitioners
v.
Paul Felzen, et al.

Docketed:
April 22, 1998 Court: United States Court of Appeals for the Seventh Circuit

Entry	Date	Proceedings and Orders
	Apr 21 1998	Petition for writ of certiorari filed. (Response due May 22, 1998)
	May 18 1998	Waiver of right of respondents Paul Felzen, et al. to respond filed.
	May 19 1998	Waiver of right of respondents Dwayne O. Andreas, et al. to respond filed.
	May 22 1998	Brief of respondents Paul Felzen, et al. in opposition filed.
	Jun 2 1998	DISTRIBUTED. June 18, 1998
	Jun 4 1998	Reply brief of petitioners California Public Employees' Retirement System, et al. filed.
	Jun 15 1998	Response requested.
	Jun 23 1998	Additional response requested -- (Due July 22, 1998).
	Jul 15 1998	Brief of respondent Directors of Archer Daniels Midland Company in opposition filed.
	Jul 22 1998	Brief of respondent Archer Daniels Midland Company in opposition filed.
	Aug 4 1998	Reply brief of petitioners California Public Employees' Retirement System, et al. filed.
	Aug 5 1998	REDISTRIBUTED. September 28, 1998
	Sep 29 1998	Petition GRANTED. limited to Question 1 presented by the petition. The brief of petitioner is to be filed with the Clerk and served upon opposing counsel on or before 3 p.m., Tuesday, November 10, 1998. The brief of respondents is to be filed with the Clerk and served upon opposing counsel on or before 3 p.m., Tuesday, December 8, 1998. A reply brief, if any, is to be filed with the Clerk and served upon opposing counsel on or before 3 p.m., Tuesday, December 29, 1998. Rule 29.2 does not apply. Justice O'Connor OUT. SET FOR ARGUMENT January 11, 1999. **********
	Nov 10 1998	Brief amici curiae of Lawrence A. Hamermesh and Mary Brigid McManamon filed.
	Nov 10 1998	Brief of petitioners California Public Employees' Retirement System, et al. filed.
	Nov 10 1998	Brief amici curiae of Barclays Global Investors, N.A., et al. filed.
	Nov 10 1998	Brief amici curiae of United States and Security Exchange Commission filed.
	Nov 10 1998	Joint appendix filed.
	Nov 10 1998	Brief amicus curiae of Council of Institutional Investors filed.
	Nov 16 1998	Motion of Public Citizen, Inc., et al. for leave to file a brief as amici curiae filed.

No. 97-1732-CFX

Entry	Date	Proceedings and Orders
	Nov 16 1998	*Typewritten motion.
	Nov 23 1998	CIRCULATED.
	Nov 27 1998	Record filed.
	Dec 4 1998	Motion of Solicitor General for leave to participate in oral argument as amicus curiae and for divided argument filed.
	Dec 8 1998	Brief of respondents Paul Felzen, et al. filed.
	Dec 8 1998	Brief of respondent Archer Daniels Midland Company filed.
	Dec 8 1998	Brief amicus curiae of Washington Legal Foundation filed.
	Dec 8 1998	LODGING consisting of an unpublished article, Conflicting Ideologies of Group Litigation, submitted by counsel for the respondent received and distributed.
	Dec 8 1998	Brief of respondents Directors of Archer Daniels Midland filed.
	Dec 14 1998	Motion of Public Citizen, Inc., et al. for leave to file a brief as amici curiae GRANTED. Justice O'Connor OUT.
	Dec 14 1998	Motion of Solicitor General for leave to participate in oral argument as amicus curiae and for divided argument GRANTED. Justice O'Connor OUT.
	Dec 29 1998	Reply brief of petitioners California Public Employees'Retirement System, et al. filed.
	Jan 11 1999	ARGUED.
	Jan 20 1999	Adjudged to be AFFIRMED. The judgment is affirmed by an equally divided Court. Opinion per curiam.

Supreme Court, U.S.
FILED
APR 29 1998
OFFICE OF THE CLERK

No. 97-1732

IN THE
Supreme Court of the United States
OCTOBER TERM, 1997

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM and FLORIDA STATE BOARD OF ADMINISTRATION,
Petitioners,

v.

PAUL FELZEN, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

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PETITION FOR A WRIT OF CERTIORARI

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62 pp

QUESTIONS PRESENTED

1. Whether a nonparty shareholder who appears, in response to notice provided under Federal Rule of Civil Procedure 23.1, to present objections to a proposed dismissal or settlement of a derivative action may appeal an adverse decision even though the shareholder has not been formally made a party to the action.

2. Whether a court of appeals may apply only prospectively a decision reversing settled precedents concerning its jurisdiction, where retroactive application would permanently foreclose appeal by a party who had reasonably relied on the prior precedents.

PARTIES TO THE PROCEEDINGS BELOW

The following persons or entities were parties to the proceedings in the court of appeals:

California Public Employees' Retirement System
Florida State Board of Administration
Paul Felzen
Louise Laskin Trust
Sandra Esner
Dwayne O. Andreas
Ralph Bruce
John H. Daniels
Howard G. Buffett
Lowell W. Andreas
James R. Randall
Michael D. Andreas
H.D. Hale
O. Glenn Webb
Martin Andreas
Margaretta Rockefeller
F. Ross Johnson
Ray A. Goldberg
Gaylord O. Coan
John K. Vanier
Shreve M. Archer, Jr.
M. Brian Mulroney
Robert S. Strauss
Archer Daniels Midland Company

PARENT COMPANIES AND NONWHOLLY OWNED SUBSIDIARIES

California Public Employees' Retirement System and Florida State Board of Administration are governmental pension funds that have no parent companies or subsidiaries that have issued shares to the public.

TABLE OF CONTENTS

	Page
QUESTIONS PRESENTED	i
PARTIES TO THE PROCEEDINGS BELOW	ii
PARENT COMPANIES AND NONWHOLLY OWNED SUBSIDIARIES	ii
TABLE OF AUTHORITIES	iv
OPINIONS BELOW	1
JURISDICTION	1
RULES INVOLVED	2
STATEMENT OF THE CASE	2
A. Background and Prior Proceedings	4
B. The Decision Below	8
REASONS FOR GRANTING THE PETITION	11
I. THE SEVENTH CIRCUIT'S DECISION CEMENTS A CIRCUIT SPLIT OF SIGNIFICANT IMPORTANCE TO ALL SHAREHOLDER DERIVATIVE SUITS, REFLECTS CONFUSION AMONG THE LOWER COURTS OVER THIS COURT'S DECISION IN *MARINO v. ORTIZ*, UNDERMINES THE PURPOSE AND DESIGN OF RULE 23.1 TO ENCOURAGE SHAREHOLDER PARTICIPATION, AND IGNORES TRADITIONAL COMMON LAW AND FEDERAL PRACTICE	11
II. THE SEVENTH CIRCUIT'S DECISION TO APPLY ITS RULING RETROACTIVELY CREATES ANOTHER CIRCUIT SPLIT, RAISES SIGNIFICANT QUESTIONS OF FEDERAL LAW, AND IS BASED ON A MISTAKEN PREMISE THAT WRONGLY INSULATES FROM APPELLATE SCRUTINY A PLAINLY COLLUSIVE SETTLEMENT IN ONE OF THE MOST SIGNIFICANT SHAREHOLDER DERIVATIVE SUITS	23
CONCLUSION	30

TABLE OF AUTHORITIES

Cases	Page
Ace Heating & Plumbing Co. v. Crane Co., 453 F.2d 30 (3d Cir. 1971)	12
Allen v. Wright, 468 U.S. 737 (1984)	28
Angoff v. Goldfine, 270 F.2d 185 (1st Cir. 1959)	21
Baldwin-United Corp., In re, 770 F.2d 328 (2d Cir. 1985)	20
Baylor v. United States Dep't of Hous. & Urban Dev., 913 F.2d 223 (5th Cir. 1990)	12
Bell Atlantic Corp. v. Bolger, 2 F.3d 1304 (3d Cir. 1993)	*passim*
Bennett v. Spear, 117 S. Ct. 1154 (1997)	27
Budinich v. Becton Dickinson & Co., 486 U.S. 196 (1988)	3, 10, 29, 30
Carlough v. Amchem Prods., Inc., 5 F.3d 707 (3d Cir. 1993)	12
Cement Antitrust Litig., In re, 688 F.2d 1297 (9th Cir. 1982), *aff'd sub nom. Arizona v. United States District Court*, 459 U.S. 1191 (1983)	12
Chevron Oil Co. v. Huson, 404 U.S. 97 (1971)	28, 29, 30
Christianson v. Colt Indus. Operating Corp., 486 U.S. 800 (1988)	10
Class Plaintiffs v. City of Seattle, 955 F.2d 1268 (9th Cir.), *cert. denied*, 506 U.S. 953 (1992)	20
Cohen v. Young, 127 F.2d 721 (6th Cir. 1942)	15
Commercial Sec. Bank v. Walker Bank & Trust Co., 456 F.2d 1352 (10th Cir. 1972)	20
Craftsman Fin. & Mortgage Co. v. Brown, 64 F. Supp. 168 (S.D.N.Y. 1945)	15
Croyden Assocs. v. Alleco, Inc., 969 F.2d 675 (8th Cir. 1992), *cert. denied*, 507 U.S. 908 (1993)	12
Daily Income Fund, Inc. v. Fox, 464 U.S. 523 (1984)	14
Dietrich Corp. v. King Resources Co., 596 F.2d 422 (10th Cir. 1979)	21
Dosier v. Miami Valley Broadcasting Corp., 656 F.2d 1295 (9th Cir. 1981)	12
EEOC v. Pan American World Airways, Inc., 897 F.2d 1499 (9th Cir.), *cert. denied*, 498 U.S. 815 (1990)	20

TABLE OF AUTHORITIES—Continued

	Page
Farmland Dairies v. Commissioner of New York State Dep't of Agric. & Markets, 847 F.2d 1038 (2d Cir. 1988)	16
Fields v. Blum, 629 F.2d 825 (2d Cir. 1980)	21
Firestone Tire & Rubber Co. v. Risjord, 449 U.S. 368 (1981)	3, 10, 24, 25
General Ins. Co. of Am. v. Eastern Consolidated Utils., Inc., 126 F.3d 215 (3d Cir. 1997)	21
General Tire & Rubber Co. Sec. Litig., In re, 726 F.2d 1075 (6th Cir.), *cert. denied*, 469 U.S. 858 (1984)	14
George v. Camacho, 119 F.3d 1393 (9th Cir. 1997)	*passim*
Gottlieb v. Wiles, 11 F.3d 1004 (10th Cir. 1993)	8, 12
Grand Jury Proceedings, In re, 654 F.2d 268 (3d Cir.), *cert. denied*, 454 U.S. 1098 (1981)	20
Guthrie v. Evans, 815 F.2d 626 (11th Cir. 1987)	12
Hal Roach Studios, Inc. v. Richard Feiner & Co., 896 F.2d 1542 (9th Cir. 1989)	20
Harper v. Virginia Dep't of Taxation, 509 U.S. 86 (1993)	23, 28, 29
Hoxworth v. Blinder, Robinson & Co., 903 F.2d 186 (3d Cir. 1990)	20
James v. Home Constr. Co. of Mobile, Inc., 689 F.2d 1357 (11th Cir. 1982)	21
James B. Beam Distilling Co. v. Georgia, 501 U.S. 529 (1991)	28
Jones v. Caddo Parish Sch. Bd., 735 F.2d 923 (9th Cir. 1984)	16
Lipscomb v. Wise, 643 F.2d 319 (5th Cir. 1981)	21
Loran v. Furr's/Bishop's Inc., 988 F.2d 554 (5th Cir. 1993)	12
Marino v. Ortiz, 484 U.S. 301 (1988)	*passim*
Marshall v. Holiday Magic, Inc., 550 F.2d 1173 (9th Cir. 1977)	12
Northern Pipeline Constr. Co. v. Marathon Pipe Line Co., 458 U.S. 50 (1982)	27
Norwood v. Slammons, 788 F. Supp. 1020 (W.D. Ark. 1991)	21

TABLE OF AUTHORITIES—Continued

	Page
PaineWebber Inc. Ltd. Partnerships Litig., In re, 94 F.3d 49 (2d Cir. 1996)	12
Papilsky v. Berndt, 466 F.2d 251 (2d Cir.), *cert. denied*, 409 U.S. 1977 (1972)	2, 14
Petersen v. Douglas County Bank & Trust Co., 967 F.2d 1186 (8th Cir. 1992)	21
Pettyjohn v. Shalala, 23 F.3d 1572 (10th Cir. 1994)	25
Pittsburgh & Lake Erie R.R. Co. Sec. & Antitrust Litig., In re, 543 F.2d 1058 (3d Cir. 1976)	15
Port Drum Co. v. Umphrey, 852 F.2d 148 (5th Cir. 1988)	21
Preston v. United States, 284 F.2d 514 (9th Cir. 1960)	21
Price v. Pelka, 690 F.2d 98 (6th Cir. 1982)	21
Ragsdale v. Turnock, 941 F.2d 501 (7th Cir. 1991), *cert. denied*, 502 U.S. 1035 (1992)	16
Rosenbaum v. MacAllister, 64 F.3d 1439 (10th Cir. 1995)	12
SEC v. Wencke, 783 F.2d 829 (9th Cir.), *cert. denied*, 479 U.S. 818 (1986)	20
Security Ins. Co. v. Schipporeit, Inc., 69 F.3d 1377 (7th Cir. 1995)	14
Sertic v. Cuyahoga, Lake, Geauga & Ashtabula Counties Carpenters Dist. Council of United Bhd. of Carpenters & Joiners, 459 F.2d 579 (6th Cir. 1972)	12
Shores v. Sklar, 844 F.2d 1485, *vacated on other grounds*, 855 F.2d 722 (11th Cir. 1988)	12
Shults v. Champion Int'l Corp., 35 F.3d 1056 (6th Cir. 1994)	12
Snyder v. Smith, 736 F.2d 409 (7th Cir.), *cert. denied*, 469 U.S. 1037 (1984)	10, 26
Stepak v. Tracinda Corp., Civil Action No. 8457, 1989 WL 100884 (Del. Ch. Aug. 18, 1989), *appeal refused*, 567 A.2d 424 (Del. 1989)	15
Thompson v. Freeman, 648 F.2d 1144 (8th Cir. 1981)	20
Tryforos v. Icarian Dev. Co., 518 F.2d 1258 (7th Cir. 1975), *cert. denied*, 423 U.S. 1091 (1976)	8, 9, 12

TABLE OF AUTHORITIES—Continued

	Page
United Airlines, Inc. v. McDonald, 432 U.S. 385 (1977)	22
United States v. Bertoli, 994 F.2d 1002 (3d Cir. 1993)	21
United States v. International Bhd. of Teamsters, 931 F.2d 177 (2d Cir. 1991)	20
United States v. Tippett, 975 F.2d 713 (10th Cir. 1992)	21
United States Catholic Conference v. Abortion Rights Mobilization, Inc., 487 U.S. 72 (1988)	21
United States ex rel. Louisiana v. Jack, 244 U.S. 397 (1917)	19
Walker v. City of Mesquite, 858 F.2d 1071 (5th Cir. 1988)	12, 13
Webcor Elecs. v. Whiting, 101 F.R.D. 461 (D. Del. 1984)	8, 16
Wolf v. Barkes, 348 F.2d 994 (2d Cir.), *cert. denied*, 382 U.S. 941 (1965)	15
Constitution, Statutes and Rules	
U.S. Const. Art. III	27
28 U.S.C. § 1254(1)	1
28 U.S.C. § 1291	22
Fed. R. App. P.:	
Rule 3	2
Rule 3(c)	21, 22
Fed. R. Civ. P.:	
Rule 23	19
Rule 23.1	*passim*
Rule 24(a)(2)	13, 14
Rule 24(b)	13
7th Cir. R. 40(e)	9
Other Materials	
Frederic Calvert, *Observations on Suits in Equity* (William Benning, 2d ed. 1846)	18
John C. Coffee, Jr., *Understanding the Plaintiff's Attorney: The Implications of Economic Theory for Private Enforcement of Law Through Class and Derivative Actions*, 86 Colum. L. Rev. 669 (1986)	5, 14

TABLE OF AUTHORITIES—Continued

	Page
Timothy A. Duffy, *The Appealability of Class Action Settlements by Unnamed Parties*, 60 U. Chi. L. Rev. 933 (1993)	13, 18
10 *Federal Procedure, Lawyers Edition* (1994)	8
5 James W. Moore, *Moore's Federal Practice* (3d ed. 1997)	8
Note, *Control Over Settlement of Shareholder's Suit*, 54 Harv. L. Rev. 833 (1941)	15
Richard A. Posner, *Economic Analysis of Law* (4th ed. 1992)	14
Roberta Romano, *The Shareholder Suit: Litigation Without Foundation?*, 7 J.L. Econ. & Org. 55 (1991)	6, 14
Joseph Story, *Commentaries on Equity Pleadings* (Little, Brown, 2d ed. 1840)	18
Charles A. Wright, *et al., Federal Practice and Procedure:*	
Vol. 7C (2d ed. 1986 & Supp. 1997)	2, 8, 15
Vol. 15A (2d ed. 1992)	13, 20, 21

IN THE

Supreme Court of the United States

OCTOBER TERM, 1997

No. ——

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM and FLORIDA STATE BOARD OF ADMINISTRATION,
Petitioners,

v.

PAUL FELZEN, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

PETITION FOR A WRIT OF CERTIORARI

California Public Employees' Retirement System ("CalPERS") and Florida State Board of Administration ("SBA") petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the Seventh Circuit.

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-10a) is reported at 134 F.3d 873. The trial court's judgment and order approving the derivative suit settlement (Pet. App. 11a-15a) is not reported.

JURISDICTION

The judgment of the court of appeals was entered on January 21, 1998. The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1).

RULES INVOLVED

The judgment of the court of appeals involves Federal Rule of Civil Procedure 23.1 and Federal Rule of Appellate Procedure 3. These provisions are set forth at Pet. App. 18a-21a.

STATEMENT OF THE CASE

This case presents two distinct circuit splits, both of which were expressly acknowledged by the Seventh Circuit. As Judge Easterbrook wrote for the panel, "[c]ourts have disagreed for several decades" over whether nonparty shareholders must formally intervene in order to appeal a derivative suit settlement. Pet. App. 2a. Reversing prior Seventh Circuit decisions on point, and disagreeing with the Third and Tenth Circuits, the panel held that formal intervention is an indispensable prerequisite to appeal. The panel also noted courts are in open "disagree[ment]" over whether decisions overruling jurisdictional precedents must always be applied retroactively. *Id.* at 10a. Again departing from prior Seventh Circuit law and contradicting the holdings of other circuits, the panel held that such decisions must be applied retroactively.

The Seventh Circuit's prohibition of appeals by nonparty shareholders eliminates a critical safeguard against collusive derivative suit settlements that benefit only plaintiffs' attorneys and defendant.[1] The court's view that it

[1] *See* 7C Charles A. Wright, *et al.*, *Federal Practice and Procedure* § 1839, at 175 (2d ed. 1986) (nonparty shareholder participation "is intended to discourage the private settlement of a derivative claim under which a shareholder-plaintiff and his attorney personally profit to the exclusion of the corporation and the other shareholders"); *Papilsky v. Berndt*, 466 F.2d 251, 258 (2d Cir.) (Nonparty shareholder participation "is essential in these situations to ensure that the [resolution] of the derivative suit is in the best interests of the corporation and the absent stockholders. More specifically, notice and court approval of settlements under Rule 23.1 discourage private settlements under which the plaintiff-stockholder and his attorney profit to the exclusion of the corporation and nonparty stockholders.") (citations omitted), *cert. denied*, 409 U.S. 1077 (1972); *see* additional authorities cited at note 14, *infra*.

was required to apply its decision retroactively ignored the important policies that encourage litigants to rely on settled law. Here, petitioners conformed their conduct to settled Seventh Circuit precedents only to have their appeal dismissed because the panel decided thereafter to change the law.[2]

These two holdings are also wrong as a matter of law. The Seventh Circuit reasoned that *Marino v. Ortiz*, 484 U.S. 301 (1988) (*per curiam*), requires nonparty shareholder intervention. But this Court in *Marino* suggested only that complete strangers to a class action should intervene before being permitted to appeal; it nowhere indicated that persons who are already privies to the proceedings—such as class members under Rule 23 or shareholders under Rule 23.1—need do so. In fact, nonparty privies *are* routinely permitted to appeal adverse decisions affecting their interests.

The court of appeals suggested that *Firestone Tire & Rubber Co. v. Risjord*, 449 U.S. 368, 379 (1981), and *Budinich v. Becton Dickinson & Co.*, 486 U.S. 196, 203 (1988), require retroactive application of its decision to limit its appellate jurisdiction because "a court may not in any case, even in the interest of justice, extend its jurisdiction where none exists." Pet. App. 9a (citation omitted). But those decisions involve statutory limits on judicial authority. The Court did not decide that purely discretionary, self-imposed restrictions on jurisdiction, such as the one imposed by the panel below, must be applied retroactively. Indeed, courts creating new and purely prudential rules narrowing their jurisdiction can and should apply such rules in a manner that is equitable.

[2] *See, e.g., George v. Camacho*, 119 F.3d 1393, 1397 (9th Cir. 1997) (*en banc*) ("The consequence of such a holding would be that litigants who complied with our rules . . . would lose their rights to appeal, . . . a result that would appear to be unconscionable to most reasoning persons whether learned in the law or not.").

A. Background and Prior Proceedings

At midnight on June 27, 1995, more than a hundred Federal Bureau of Investigation ("FBI") agents raided ADM corporate headquarters and the homes of ADM top executives. The next day, ADM issued a press release announcing that three separate federal grand juries were investigating whether the company's officers had conspired with rivals to fix artificially high prices for citric acid, high fructose corn syrup, and lysine. The evidence the government amassed proved overwhelming: the FBI had obtained audio tapes, video tapes, and documents establishing that ADM executives had conspired with at least three foreign companies to set prices and production quotas. On October 15, 1996, ADM pleaded guilty to criminal antitrust charges and paid a $100 million criminal fine, the largest criminal antitrust fine ever imposed and the subject of national media attention. Settling three civil antitrust lawsuits filed by ADM competitors cost the company another $90 million.

Petitioners CalPERS and SBA are two of the largest public pension funds in the United States. They have combined assets of nearly $200 billion and are among the largest shareholders of ADM stock. SBA owns over 1.7 million ADM shares; CalPERS owns over 2.9 million shares.

In response to the demands of institutional shareholders like CalPERS and SBA and waves of negative publicity, ADM commissioned a report to propose new, more stringent corporate governance measures. Much of ADM's troubles, in the view of shareholders and the public, lay in the personal, professional, familial, and financial connections between the members of the company's board charged with management oversight. Indeed, in October 1995, CalPERS awarded ADM a grade of "F" for its lack of corporate governance principles.

The report ADM eventually issued and adopted in January 1996, however, did little to alleviate shareholder

concern. For instance, while it required (for the first time) that ADM's board include at least a majority of independent members, even persons having obvious and substantial financial ties to ADM could qualify under the new rules as "independent." To remedy that defect and avoid a return to the corporate cronyism that resulted in ADM's criminal plea, CalPERS and SBA submitted a shareholder proposal that no one with personal or financial ties to the company could serve as an "independent" director. They modeled their proposal on accepted standards for corporate independence developed by the Council of Institutional Investors (the "Council").[3] The Council is an association of more than one hundred corporate, public, and union pension funds devoted to addressing their members' investment concerns and promoting responsible corporate governance rules and procedures. Although vehemently opposed by management, the shareholders' proposal still won 41.6 percent of the vote at the 1996 shareholder meeting.

Unsurprisingly, in the wake of the federal criminal probe and continuing publicity, plaintiffs' lawyers dashed to the courthouse to file shareholder derivative actions against ADM directors.[4] Various actions were filed in two states, and all were eventually consolidated in the Central District of Illinois. The consolidated suit alleged that ADM directors had breached their fiduciary duties to stockholders by failing to supervise company employees properly, and sought recovery of the $190 million the company had

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[3] The Council's independence standards have been adopted by most or many of the nation's largest companies. The Council is a deliberative organization that adopts policies only based on essentially unanimous votes among its institutional shareholder members.

[4] "[A]vailable empirical evidence suggests that [derivative] actions regularly follow in the wake of prior proceedings by the SEC or other governmental agencies." John C. Coffee, Jr., *Understanding the Plaintiff's Attorney: The Implications of Economic Theory for Private Enforcement of Law Through Class and Derivative Actions*, 86 Colum. L. Rev. 669, 673 n.9 (1986).

been forced to pay in criminal fines and civil settlements. Indeed, plaintiffs' attorneys touted in writing to the Council that "a primary goal of our litigation is to recover for ADM as much of the wasted $190 million as is realistically and reasonably possible." Objections of CalPERS and SBA to Proposed Settlement of Derivative Action (July 2, 1997), Exh. A at 2 (attaching letter).

Plaintiffs' counsel, however, did almost nothing to prosecute the case. Nearly two years after filing, they still had not fully litigated defendants' motion to dismiss. By their own admission, they had also neglected to seek any meaningful discovery. In fact, plaintiffs' lawyers focused what little energy they expended on settlement with the insurance company for ADM's executives. In the resulting agreement ("Settlement"), reached on May 29, 1997, plaintiffs' attorneys agreed to release "any and all causes of action" against ADM and the director defendants in return for a mere $8 million settlement fund—less than 4.3 percent of the sought-after $190 million.

The parties then went on to allocate the fund *exclusively* to pay attorneys' fees. Half was earmarked for paying the attorneys bringing suit.[5] The other half was designated for payment of future legal fees incurred by ADM in attempting to reform itself.[6] Not one dime was returned to the corporation for shareholders who lost $190 million in value as a result of their fiduciaries' misconduct.

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[5] The parties signed a so-called "free sailing provision" under which defendants agreed not to oppose a fee petition seeking to direct $3.92 million, or 49 percent of the fund, to plaintiffs' counsel (plus interest, coming out of the remaining 51 percent). The average fee award in shareholder derivative suits where no monetary settlement is made (effectively the case here) is $287,000. Roberta Romano, *The Shareholder Suit: Litigation Without Foundation?*, 7 J.L. Econ. & Org. 55, 63 (1991). Even in cases where monetary settlements are made to shareholders, fee awards average no more than 24 percent of the settlement amount. *Id.*

[6] Adding to the conflict of interest, plaintiffs' attorneys remained eligible under the settlement to earn these fees as well.

The Settlement also endorsed the "reform" measures voluntarily adopted by ADM a year earlier. Though plaintiffs crowed that they had "extracted" concessions beyond ADM's self-imposed reforms, fine-print details revealed the opposite; for instance, plaintiffs did almost nothing to address the question of director independence, the single most important reform measure and the one that had nearly passed at the previous shareholder meeting over management opposition.

After executing the Settlement, and without notice to shareholders, the parties appeared before the district court and obtained an order on May 30, 1997, tentatively approving their agreement. Pursuant to the last sentence in Rule 23.1, the district court at that point invited "[a]ny shareholder of record of ADM" to "appear and show cause, if he, she or it has any [reason] why the proposed settlement of the derivative claims . . . should or should not be entered thereon." Order Preliminarily Approving Settlement and Providing for Notice at 3 (May 30, 1997).[7] The court set a deadline of July 3, 1997, for written objections and scheduled a final settlement hearing for July 7, 1997.

In response to the court's invitation, petitioners filed written objections, accepted by the district court, and appeared at the July 7 hearing. Petitioners asked the court to reject the Settlement on the ground that the cash benefit to plaintiffs' lawyers was disproportionately high and the corporate governance "concessions" provided no material benefit to shareholders beyond what ADM had itself adopted a year earlier. Alternatively, petitioners asked the court to order the parties to show cause why corporate governance provisions should not be revised to require truly independent directors. Nevertheless, at the

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[7] Rule 23.1 provides in pertinent part that "[t]he action shall not be dismissed or compromised without the approval of the court, and notice of the proposed dismissal or compromise shall be given to shareholders or members in such manner as the court directs."

conclusion of the hearing the district court approved the Settlement. Petitioners appealed to the Seventh Circuit.

B. The Decision Below

The panel refused to hear petitioners' appeal, left them unable *ever* to appeal the collusive ADM settlement, overruled several circuit cases in the process, and expressly recognized that its decision created two direct conflicts with the considered decisions of other circuits.

1. In *Tryforos v. Icarian Development Co.*, 518 F.2d 1258 (7th Cir. 1975), *cert. denied*, 423 U.S. 1091 (1976), then-Judge Stevens held that "[t]he law is clear that a non-party shareholder who appears, pursuant to a Rule 23.1 notice, to present objections to a proposed dismissal or settlement of a derivative action may appeal an adverse decision even though he has not been formally made a party to the action." *Id.* at 1263 n.22. This view has been endorsed by other circuits. *See, e.g., Bell Atlantic Corp. v. Bolger*, 2 F.3d 1304 (3d Cir. 1993) (Scirica, J.); *Gottlieb v. Wiles*, 11 F.3d 1004, 1011 (10th Cir. 1993) (McKay, C.J.). It has been approved by leading commentators.[8] And some courts have even expressed displeasure at shareholder motions to intervene. *See, e.g., Webcor Elecs. v. Whiting*, 101 F.R.D. 461, 463 (D. Del. 1984) (complaining that motion to intervene was "superfluous procedural question" since nonparty objector already had standing to appeal).

With *Tryforos* as direct on-point authority guaranteeing nonparty objectors' right to appeal, and with so many other authorities in concurrence, petitioners did not seek

[8] *See, e.g.*, 7C Wright, *supra*, § 1839, at 182 (2d ed. 1986 & Supp. 1997) ("objector to the settlement may appeal the court's approval of the compromise"); 5 James W. Moore, *Moore's Federal Practice* ¶ 23.1.10[3] (3d ed. 1997) (same); 10 *Federal Procedure, Lawyers Edition* § 25:184, at 260 (1994) ("nonparty shareholder who appears, pursuant to an FRCP 23.1 notice, to present objections to a proposed dismissal or settlement of a derivative action may appeal an adverse decision without having been formally made a party to the action").

leave to intervene in the trial court. The Seventh Circuit panel, however, expressly overruled *Tryforos*, disagreed with the Third Circuit's decision in *Bell Atlantic*, and held formal intervention to be an absolute prerequisite to appeal. Pet. App. 1a-4a.[9]

The panel based its ruling almost entirely on a gloss of inessential language from this Court's intervening *per curiam* opinion in *Marino*. There the Court commented that it is "better practice" to require nonparties to intervene formally before allowing them to appeal. 484 U.S. at 304. From that single aside, the court of appeals inferred that both nonparty class members under Rule 23 and nonparty shareholders under Rule 23.1 *must always* intervene in order to appeal.

The panel stated that its conclusion required it to overrule *Tryforos* and split with other recent circuit decisions. Pet. App. 6a-7a (acknowledging that Third Circuit "has held, despite *Marino*, that a shareholder need not become a party in order to appeal from the final decision in derivative litigation"); *id.* at 2a ("[c]ourts have disagreed for several decades about whether class members (and shareholders, their counterparts in derivative actions under Rule 23.1) must intervene"); *id.* at 4a ("we now formally overrule . . . any . . . case in this circuit . . . that permits non-parties to appeal").

2. The court of appeals next turned to the question whether to apply its decision retroactively to petitioners. The court acknowledged that retroactive application of its intervention requirement would preclude petitioners from *ever* appealing the ADM settlement—and would do so despite the fact that they had followed all proper procedures under settled Seventh Circuit law at the time they appealed. *Id.* at 7a-10a.

[9] Pursuant to Seventh Circuit Rule 40(e), the panel overruled its prior precedent by circulating its opinion to all circuit judges in active service prior to its release. Pet. App. 10a.

The court concluded that it was bound to apply its new intervention requirement to CalPERS and SBA, unfairness notwithstanding, because of language in *Firestone* (and subsequently reiterated in *Budinich* and *Christianson v. Colt Industries Operating Corp.*, 486 U.S. 800, 818 (1988)): "A court lacks discretion to consider the merits of a case over which it is without jurisdiction, and thus, by definition, a jurisdictional ruling may never be made prospective only." *Firestone*, 449 U.S. at 379. Because this case "concern[ed] jurisdiction[al]" prerequisites to appeal, Judge Easterbrook reasoned, the court's new rule had to be applied retroactively to bar the appeal of CalPERS and SBA. Pet. App. 8a-9a.

The panel acknowledged that this second holding also overruled a Seventh Circuit precedent (*Snyder v. Smith*, 736 F.2d 409 (7th Cir.), *cert. denied*, 469 U.S. 1037 (1984)) and created another direct circuit split—this time with the Ninth Circuit's decision in *George v. Camacho*, 119 F.3d at 1399. Pet. App. 10a ("overrul[ing] *Snyder* and disagree[ing] with *George*"). Just last year the Ninth Circuit, sitting *en banc*, held that nothing in *Firestone* or its progeny required retroactive application of new jurisdictional rules where such application would bar appellants from ever raising their issues on appeal. *George*, 119 F.3d at 1399. Until this case, the Seventh Circuit had taken the same view, stating that *Firestone* "did not address the issue of whether an appellate court must dismiss the appeal where a party who relies on a jurisdictional ruling is, under a subsequent decision, foreclosed from ever raising his issues in the appellate court." *Snyder*, 736 F.2d at 415.

REASONS FOR GRANTING THE PETITION

I. THE SEVENTH CIRCUIT'S DECISION CEMENTS A CIRCUIT SPLIT OF SIGNIFICANT IMPORTANCE TO ALL SHAREHOLDER DERIVATIVE SUITS, REFLECTS CONFUSION AMONG THE LOWER COURTS OVER THIS COURT'S DECISION IN *MARINO v. ORTIZ*, UNDERMINES THE PURPOSE AND DESIGN OF RULE 23.1 TO ENCOURAGE SHAREHOLDER PARTICIPATION, AND IGNORES TRADITIONAL COMMON LAW AND FEDERAL PRACTICE

As Judge Easterbrook noted, the lower federal courts are irreconcilably split over whether nonparty shareholders must intervene as parties in order to appeal adverse judgments. Pet. App. 2a. This split has substantial consequences for all nonparty shareholders and the vitality of the shareholder derivative suit process itself. It leaves objecting shareholders uncertain of their rights, effectively prevents *any* shareholder appeals in the Seventh Circuit, and invites forum shopping.

The Seventh Circuit reasoned that its ruling was compelled by this Court's *per curiam* decision in *Marino v. Ortiz*, 484 U.S. 301 (1988). But Judge Easterbrook acknowledged that the Third Circuit disagrees. Pet. App. 6a-7a (conceding disagreement with Third Circuit's view of *Marino*). The Third Circuit's view is correct. The court's decision below undermines the purposes of Rule 23.1, diverges from traditional common law and federal practice, and finds no support in *Marino*, which dealt only with the right of complete outsiders to contest a class action settlement between willing class members and the defendants.

A. The panel below virtually invited certiorari, noting at the outset of its opinion that "[c]ourts have disagreed for several decades about whether class members (and shareholders, their counterparts in derivative actions under Rule 23.1) must intervene as parties in order to appeal from adverse decisions." Pet. App. 2a. Resolution of

lower court disputes over questions of federal law is a central function of this Court's certiorari jurisdiction.

Nor can the split of authority be reconciled. The Third, Tenth, and (until now) Seventh Circuits have all approved nonparty shareholder appeals. *See, e.g., Bell Atlantic Corp. v. Bolger*, 2 F.3d 1304; *Gottlieb v. Wiles*, 11 F.3d 1004; *Rosenbaum v. MacAllister*, 64 F.3d 1439 (10th Cir. 1985); *Tryforos v. Icarian Dev. Co.*, 518 F.2d 1258. The Seventh Circuit now demands formal intervention, in express "disagree[ment]" with these courts. Pet. App. 7a.[10]

The fracture has been compounded by a lone paragraph in *Marino*. *See* Pet. App. 1a-2a. Some courts, like

[10] This same split is mirrored in the context of Federal Rule of Civil Procedure 23 class actions. Several circuits hold that nonparty class members need not intervene before appealing. *See, e.g., In re PaineWebber Inc. Ltd. Partnerships Litig.*, 94 F.3d 49 (2d Cir. 1996); *Carlough v. Amchem Prods., Inc.*, 5 F.3d 707, 713-14 (3d Cir. 1993); *Ace Heating & Plumbing Co. v. Crane Co.*, 453 F.2d 30, 32 (3d Cir. 1971); *Shults v. Champion Int'l Corp.*, 35 F.3d 1056 (6th Cir. 1994); *Sertic v. Cuyahoga, Lake, Geauga & Ashtabula Counties Carpenters Dist. Council of United Bhd. of Carpenters & Joiners*, 459 F.2d 579 (6th Cir. 1972); *In re Cement Antitrust Litig.*, 688 F.2d 1297, 1309 (9th Cir. 1982), *aff'd sub nom. Arizona v. United States District Court*, 459 U.S. 1191 (1983); *Dosier v. Miami Valley Broadcasting Corp.*, 656 F.2d 1295, 1299 (9th Cir. 1981); *Marshall v. Holiday Magic, Inc.*, 550 F.2d 1173, 1176 (9th Cir. 1977).

Others hold that intervention is required. *See, e.g., Loran v. Furr's/Bishop's Inc.*, 988 F.2d 554, 554 (5th Cir. 1993) ("[W]e have no jurisdiction to consider an appeal by a class member who has not attempted to intervene as a named party."); *Baylor v. United States Dep't of Hous. & Urban Dev.*, 913 F.2d 223, 225 (5th Cir. 1990); *Walker v. City of Mesquite*, 858 F.2d 1071, 1073-74 (5th Cir. 1988); *Croyden Assocs. v. Alleco, Inc.*, 969 F.2d 675 (8th Cir. 1992), *cert. denied*, 507 U.S. 908 (1993); *Shores v. Sklar*, 844 F.2d 1485, 1491, *vacated on other grounds*, 855 F.2d 722 (11th Cir. 1988); *Guthrie v. Evans*, 815 F.2d 626, 628 (11th Cir. 1987).

Whatever result the Court reaches in this case in the context of Rule 23.1 shareholder derivative suits will also provide much-needed guidance to the lower courts in the context of Rule 23 class actions.

the Seventh Circuit, read this passage as confirming (and even mandating) their decision to bar nonparty shareholder appeals. *See id.* Others see this language as horatory and not addressed to nonparty shareholders. *See, e.g., Bell Atlantic*, 2 F.3d at 1307, 1308 & n.6 (noting that *Marino* purported to describe "better practice" regarding appellants who were not even members of the affected class); *Gottlieb*, 11 F.3d at 1011 (adopting *Bell Atlantic*).[11] The intercircuit dispute over the effect of *Marino* provides further grounds for granting certiorari.[12]

B. The circuits' split over intervention has tremendous practical consequences for all nonparty shareholders and the integrity of the shareholder derivative suit process.

In some courts, nonparty shareholders have an absolute *right* to appeal any collusive settlement. In others, like the Seventh Circuit, their ability to appeal now turns on a purely *discretionary* decision by the trial court.[13] The

[11] *See also* 15A Wright, *supra*, § 3902.1, at 122 (2d ed. 1992) ("The justification for recognizing appeal standing in some of these [nonparty] cases is so compelling as to justify putting aside any formal requirement of intervention, though the 'better practice' is to seek intervention in the district court.") (quoting *Marino*); Timothy A. Duffy, *The Appealability of Class Action Settlements by Unnamed Parties*, 60 U. Chi. L. Rev. 933, 946 (1993) ("[L]ower courts have not taken *Marino* as proffering an unqualified command; they have decided that a non-party may sometimes appeal without prior intervention.").

[12] Disagreement over *Marino* has also contributed to the split of authority over intervention in the Rule 23 class action context. *See, e.g., Walker*, 858 F.2d at 1074 (Fifth Circuit refusing nonparty class member appeal because of *Marino*); *Croyden*, 969 F.2d at 679-80 (same holding in Eighth Circuit). Thus, clarifying *Marino*'s meaning here will also contribute to resolving the class action split.

[13] Under Rule 24(b), "permissive intervention" is expressly left to the "discretion" of the trial court. Fed. R. Civ. P. 24(b). Even if intervention here is considered "of right" under Rule 24(a)(2), the district court is still granted wide discretionary power to determine whether "the applicant is so situated that the disposition of the action may as a practical matter impair or impede" its rights, and whether the applicant's interests are already

federal courts rarely disagree over a question so central to the administration of justice as the right to appellate review for an entire class of persons.

A key procedural safeguard against collusion and abuse is also at stake in the lower court's split. In all derivative litigation, strong economic incentives tempt plaintiffs' counsel and defendants to "structure a settlement such that the plaintiffs' attorneys' fees are disproportionate to any relief obtained for the corporation." *Bell Atlantic*, 2 F.3d at 1310.[14] Courts and commentators have long considered participation by nonparty shareholders in the judicial settlement review process to be a key procedural countermeasure for exposing and preventing such corruption.[15]

"adequately represented" by the parties. Fed. R. Civ. P. 24(a)(2). *See also Security Ins. Co. v. Schipporeit, Inc.*, 69 F.3d 1377, 1380 (7th Cir. 1995) (deciding whether to permit intervention "of right" requires trial court to apply four-part balancing test). Worse still, some courts have suggested that objecting shareholders' interests are necessarily "adequately protected" by party shareholders in Rule 23.1 suits. *See, e.g., In re General Tire & Rubber Co. Sec. Litig.*, 726 F.2d 1075, 1087 (6th Cir.), *cert. denied*, 469 U.S. 858 (1984).

[14] *See also id.* at 1309 n.8 & 1310 n.10 (citing, *inter alia*, Richard A. Posner, *Economic Analysis of Law* § 21.9, at 570 (4th ed. 1992) (plaintiffs' attorney "will be tempted to offer to settle with defendant for a small judgment and a large legal fee, and such an offer will be attractive to the defendant provided the sum of the two figures is less than the defendant's net expected loss from going to trial"); Romano, 7 J.L. Econ. & Org. at 57 (combination of differential indemnification rights, insurance policy exclusions, plaintiffs' counsel's interest in fees, and individual defendants' risk aversion creates powerful and potentially perverse incentives to settle); Coffee, 86 Colum. L. Rev. at 677 (derivative suits "are uniquely vulnerable to collusive settlements that benefit plaintiff's attorneys rather than their clients")).

[15] *See, e.g., Daily Income Fund, Inc. v. Fox*, 464 U.S. 523, 532 n.7 (1984) ("[T]he provision requiring notice and court approval of settlements [is] also intended to prevent shareholders from suing in place of the corporation in circumstances where the action would disserve the legitimate interests of the company or its shareholders."); *Papilsky*, 466 F.2d at 258 ("[n]otice is essential in these situations to ensure that the [resolution] of the derivative suit is

Replacing nonparty shareholders' longstanding *right* to appeal a settlement on the merits with a discretionary *chance* to appeal reduces their ability to serve that monitoring function. It also raises the costs (and thus reduces the likelihood) of their participation. Simply to provide their views on the fairness of a settlement, nonparty shareholders are faced with the substantial added financial burden of litigating an intervention motion (and possibly an appeal of the district court's denial of leave to intervene).

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in the best interests of the corporation and the absent stockholders") (citations omitted); *Wolf v. Barkes*, 348 F.2d 994, 996 n.2 (2d Cir.) (Friendly, J.) (that ensuring nonparty oversight and participation "was the objective" of the Rule "is indicated by the [1937] Advisory Committee's citation of McLaughlin, Capacity of a Plaintiff-Stockholder to Terminate a Stockholder's Suit, 46 Yale L.J. 421, 430 (1936)," in its commentary to what was then Rule 23(c), now Rule 23(e)), *cert. denied*, 382 U.S. 941 (1965); *Bell Atlantic*, 2 F.3d at 1310 ("objectors play an important role by giving courts access to information on the settlement's merits"); *In re Pittsburgh & Lake Erie R.R. Co. Sec. & Antitrust Litig.*, 543 F.2d 1058, 1069-70 (3d Cir. 1976) (holding that nonparties may appeal where their "equity is being diluted," since their "distinctive interests are as worthy of consideration and protection as [party] shareholders"); *Cohen v. Young*, 127 F.2d 721 (6th Cir. 1942) (nonparty shareholder participation key "in order that the court may have the benefit of that broader information which comes from receiving advice as to the views of all parties concerned"); *Craftsman Fin. & Mortgage Co. v. Brown*, 64 F. Supp. 168, 178 (S.D.N.Y. 1945) (nonparty shareholder participation key to remedy the "evil" of "private settlements under which the plaintiff stockholder and his attorney got the sum paid in settlement, and the corporation got nothing"); *Stepak v. Tracinda Corp.*, Civil Action No. 8457, 1989 WL 100884, at *1 (Del. Ch. Aug. 18, 1989) (objectors' "ardent[] resist[ance] [to] the settlement" persuaded court "to look more closely at the proposal than would ordinarily be the case"; as a result of objector participation, court concluded there was "no reasonable likelihood that the proposed settlement would be approved as fair and reasonable"), *appeal refused*, 567 A.2d 424 (Del. 1989) (Table); 7C Wright, *supra*, § 1839, at 175 (nonparty shareholder participation "is intended to discourage the private settlement of a derivative claim under which a shareholder-plaintiff and his attorney personally profit to the exclusion of the corporation and the other shareholders"); Note, *Control Over Settlement of Shareholder's Suit*, 54 Harv. L. Rev. 833 (1941).

They are faced, too, with all the costs and inconveniences associated with party status, including wide-ranging automatic disclosure obligations and the obligation to respond to interrogatories, appear for deposition, and answer virtually unlimited demands for documents. Increasing barriers to (and costs of) nonparty participation concomitantly increases the parties' incentives to collude—as well as the likelihood that flawed settlements will survive judicial scrutiny.[16]

Resolution of this split is important for other reasons. Under current law, whether intervention is required differs from jurisdiction to jurisdiction, leaving shareholder litigants uncertain of their appellate rights and the procedures they need to follow to preserve those rights. Failing to bring a formal motion to intervene is a fatal error in some courts; in others, such a motion is treated as an unwelcome and wasteful formalism. *Cf. Webcor Elecs.*, 101 F.R.D. at 463; *see* p. 8, *supra*.[17] Further, in circuits where nonparties can appeal only after intervening, they are typically notified of their right to object and participate only *after* the parties have reached a tentative settlement. *See* note 7, *supra*. Yet, settled law in the Seventh Circuit and elsewhere strongly *disfavors* intervention after a tentative settlement is reached.[18] As a practical matter, the intervention requirement makes appeal of

[16] Many commentators have already called on Congress for abolition of derivative suits as too prone to collusion. *See* Pet. App. 6a (citing articles). This view is also expressed in the panel's decision below. *Id.*

[17] Worse still, even when shareholders carefully follow all applicable law in jurisdictions that do not require intervention, they risk being whipsawed (like petitioners here) by the court of appeals reversing itself, changing sides in the ongoing split, and foreclosing a shareholder appeal that was proper under prior law.

[18] *See, e.g., Farmland Dairies v. Commissioner of New York State Dep't of Agric. & Markets*, 847 F.2d 1038, 1043-44 (2d Cir. 1988); *Jones v. Caddo Parish Sch. Bd.*, 735 F.2d 923 (5th Cir. 1984); *Ragsdale v. Turnock*, 941 F.2d 501, 504 (7th Cir. 1991), *cert. denied*, 502 U.S. 1035 (1992).

a flawed derivative settlement highly unlikely, if not impossible.

Finally, shareholder derivative suits are amenable to jurisdiction almost anywhere in the United States (plaintiffs' attorneys can usually find a shareholder willing to serve as plaintiff in the jurisdiction of choice). The current, chaotic state of the law encourages a perverse form of forum shopping. Those seeking quick, quiet (and collusive) derivative settlements that benefit them—and not the company—will have a strong incentive to file where intervention is required and where appellate review of any collusive settlement is therefore unlikely.

C. The Seventh Circuit's shareholder intervention mandate is wrong as a matter of law. Its error directly affects the quality of the judicial oversight and review process in the many derivative actions handled by the federal courts.

Under Rule 23.1, nonparty shareholders are entitled to appear and contest any proposed settlement; unlike purely private suits, intervention is not required for nonparties to participate in the trial court. Rule 23.1 was deliberately drafted in this manner to encourage maximum nonparty shareholder participation. "[O]bjectors play an important role by giving courts access to information on the settlement's merits." *Bell Atlantic*, 2 F.3d at 1310; *Papilsky*, 466 F.2d at 258 (shareholder participation is "essential in these situations to ensure that the [resolution] of the derivative suit is in the best interests of the corporation and the absent stockholders"); *see also* authorities cited at note 15, *supra*.

The Seventh Circuit's newly fashioned rule is inconsistent with the purposes of Rule 23.1. It raises the costs for nonparties to participate, reduces their ability to appeal, and creates new incentives to collude. It also reduces the likelihood that the court of appeals will have all the information necessary to assess the fairness of a settlement. The Third Circuit expressly refused to mandate intervention for just these reasons. *Bell Atlantic*, 2 F.3d

at 1310 (Rule's goal of preventing collusive settlements "cautions against creating obstacles to challenging derivative action settlement agreements"). *See also Gottlieb*, 11 F.3d at 1011 (same); Duffy, 60 U. Chi. L. Rev. at 951 (requiring intervention is inconsistent with "the rule that encourages settlement to a reasonable degree, and also encourages fair settlements").

The Seventh Circuit's decision is also in tension with common law practice. *See generally* Duffy, 60 U. Chi. L. Rev. at 942. English legal scholar Fredric Calvert argued as early as 1846 that the British common law had already provided unnamed class members the right to appeal for over a hundred years. *See id.* at 940-41 (discussing Frederic Calvert, *Observations on Suits in Equity* 38 (William Benning, 2d ed. 1846)). And Calvert himself defended this right at length: "[T]he privilege of appeal [in class action suits] ought to be given in such a manner as to induce the readiest acquiescence in the system of representation during the earlier part of the suit; for which reason every individual ought, as it appears to me, to . . . have the power of appealing, whether he has been a suitor . . . or by some other person as his representative." *Id.* In America, Joseph Story reiterated Calvert's position in his *Commentaries on Equity Pleadings*, arguing that, where affected individuals are too numerous to appear in court, "they may come in under the decree, and take the benefit of it, or show it to be erroneous, or entitle themselves to a rehearing." *Id.* at 941 (quoting Joseph Story, *Commentaries on Equity Pleadings* 96 (Little, Brown, 2d ed. 1840)).

The Seventh Circuit rested its decision not on any disagreement over the importance of nonparty oversight, any different view about Rule 23.1's purpose, or any contrary understanding of common law practice. Instead, it concluded that three sentences from *Marino* controlled:

> The rule that only parties to a lawsuit, or those that properly become parties, may appeal an adverse judgment, is well settled. The Court of Appeals suggested that there may be exceptions to this general rule, primarily "when the nonparty has an interest that is affected by the trial court's judgment." We think the better practice is for such a nonparty to seek intervention for purposes of appeal . . . .

484 U.S. at 304 (citations omitted).

The Seventh Circuit's single-minded reliance on *Marino* is misplaced.

First, the quoted language is unnecessary to *Marino*'s *per curiam* holding. It discusses only "better practice," and does not set out an exceptionless rule for all cases. Other courts and leading commentators have recognized this point. *See, e.g., Bell Atlantic*, 2 F.3d at 1307; note 11, *supra*.

Second, the nonparties seeking to appeal in *Marino* were not even members of the class at issue, but outsiders with no right to participate in trial court proceedings under Rule 23. They were white police officers seeking to challenge a class action settlement between black officers and the police authorities. Nothing in *Marino* addressed the appellate rights of nonparties who *are* members of the class whose rights *are* directly affected by any judgment entered in the case, and who have an express right under the federal rules to participate in trial court proceedings without intervention. *Bell Atlantic*, 2 F.3d at 1308 n.6.

The lone case cited in the pertinent passage in *Marino* confirms this conclusion. *United States ex rel. Louisiana v. Jack*, 244 U.S. 397 (1917), cited in *Marino*, 484 U.S. at 304, involved a land dispute between a state agency and a landowner; the State of Louisiana sought to participate in the proceedings. The Court held the State not a proper party and explained that "it has long been the law" that "part[ies] *and priv*[*ies*] *to the record*" may appeal an adverse decision, though even to this rule the Court acknowledged some "exceptions." 244 U.S. at 402 (emphasis added). There is no doubt that nonparty share-

holders are at least "privy to the record" in derivative suits.[19]

Third, if *Marino held* that "only parties to a lawsuit, or those that properly become parties, may appeal" (484 U.S. at 304), much settled law would have to be overturned. Nonparties affected by trial court judgments are treated by the federal courts as "de facto" parties and permitted to appeal without intervention in a "surprising range" of circumstances. 15A Wright, *supra*, § 3902.1, at 102.[20] For instance, federal courts routinely permit nonparty appeals from judgments that bind the nonparty by name. *Id.* at 122 (citing cases).[21] They permit nonparty witnesses held in contempt for refusing discovery to appeal on claims of privilege, lack of personal jurisdiction, and other matters. *See* 15A Wright, § 3902.1, at

[19] The Seventh Circuit virtually conceded as much. Pet. App. 7a ("The third circuit conceived of the question as whether the shareholder has standing, which is misleading. Standing means injury in fact, and a reduction in the market price of one's stock is injury.").

[20] *See id.* at 122 (collecting examples and commenting that "Nonparties need not always go through a formal intervention procedure to achieve standing to appeal. Appeals have been permitted on showings that range from easy cases in which a nonparty is formally addressed by a court order through less clear cases in which a nonparty is significantly affected.").

[21] *See also United States v. International Bhd. of Teamsters*, 931 F.2d 177, 183-84 (2d Cir. 1991); *In re Baldwin-United Corp.*, 770 F.2d 328, 335 (2d Cir. 1985); *Hoxworth v. Blinder, Robinson & Co.*, 903 F.2d 186, 194 n.12 (3d Cir. 1990); *In re Grand Jury Proceedings*, 654 F.2d 268, 270-71 (3d Cir.), *cert. denied*, 454 U.S. 1098 (1981); *Thompson v. Freeman*, 648 F.2d 1144, 1147 n.5 (8th Cir. 1981); *Class Plaintiffs v. City of Seattle*, 955 F.2d 1268, 1277-78 (9th Cir.), *cert. denied*, 506 U.S. 953 (1992); *EEOC v. Pan American World Airways, Inc.*, 897 F.2d 1499, 1504 (9th Cir.), *cert. denied*, 498 U.S. 815 (1990); *Hal Roach Studios, Inc. v. Richard Feiner & Co.*, 896 F.2d 1542, 1546-47 (9th Cir. 1989); *SEC v. Wencke*, 783 F.2d 829, 834 (9th Cir.), *cert. denied*, 479 U.S. 818 (1986); *Commercial Sec. Bank v. Walker Bank & Trust Co.*, 456 F.2d 1352, 1354 (10th Cir. 1972).

124.[22] They regularly allow attorneys and expert witnesses to appeal district court denials of fees. *See* 15A Wright, § 3902.1, at 126 & n.45.[23] And nonparties obligated to reimburse the defendant for amounts paid under the trial court's judgment are also heard on a routine basis. *See* 15A Wright, § 3902.1, at 127 & n.47.[24] There is nothing in *Marino* to suggest that its reference to "better practice" was intended to sweep away such a vast body of federal law. Nor is there any basis in *Marino* or the Seventh Circuit's decision to justify denying injured nonparty shareholders the right to appeal when these other nonparties are routinely heard.

Beyond *Marino*, the only other authority the Seventh Circuit cited for terminating nonparty shareholder appeals is Federal Rule of Appellate Procedure 3(c). Pet. App. 2a. Rule 3(c), the panel emphasized, provides that "[a] notice of appeal must specify the *party or parties* taking the appeal by naming each appellant in either the caption or the body of the notice of appeal." (emphasis added).

[22] *See also United States Catholic Conference v. Abortion Rights Mobilization, Inc.*, 487 U.S. 72, 76 (1988); *General Ins. Co. of Am. v. Eastern Consolidated Utils., Inc.*, 126 F.3d 215, 218 (3d Cir. 1997); *United States v. Bertoli*, 994 F.2d 1002, 1012 (3d Cir. 1993); *Port Drum Co. v. Umphrey*, 852 F.2d 148, 150 n.2 (5th Cir. 1988); *Petersen v. Douglas County Bank & Trust Co.*, 967 F.2d 1186, 1188 (8th Cir. 1992); *Norwood v. Slammons*, 788 F. Supp. 1020, 1024 (W.D. Ark. 1991).

[23] *See also Angoff v. Goldfine*, 270 F.2d 185, 186 (1st Cir. 1959); *Lipscomb v. Wise*, 643 F.2d 319, 320-21 (5th Cir. 1981); *Price v. Pelka*, 690 F.2d 98, 102 (6th Cir. 1982); *Preston v. United States*, 284 F.2d 514, 515 n.1 (9th Cir. 1960); *United States v. Tippett*, 975 F.2d 713, 718 (10th Cir. 1992); *Dietrich Corp. v. King Resources Co.*, 596 F.2d 422, 424 (10th Cir. 1979); *James v. Home Constr. Co. of Mobile, Inc.*, 689 F.2d 1357, 1359 (11th Cir. 1982).

[24] *See also Fields v. Blum*, 629 F.2d 825, 827 (2d Cir. 1980) (order enjoining reduction of welfare benefits by city official could be appealed by state, since state was legally required to reimburse city for payments and controlled both the activities complained of and the conduct of local officials).

Because no party is taking the appeal here, the Seventh Circuit reasoned, it must be improper under Rule 3(c). *Id.*

This is far too thin a reed on which to rest such a weighty result. The Seventh Circuit's reading of Rule 3(c) would bar not just nonparty shareholder appeals, but *all* nonparty appeals, a distinctly unlikely result given longstanding acceptance of such appeals. *See* notes 21-24, *supra*. Besides, Rule 3(c) hardly purports to delineate what matters are inherently eligible or ineligible for appeal. That is the domain of Article III jurisprudence and 28 U.S.C. § 1291, neither of which purports to restrict appellate jurisdiction to parties alone.[25] On its face, Rule 3(c) is concerned only with the formal "content[s] of the notice of appeal." It simply ensures that sufficient information appears on the face of the notice for the court of appeals to discern the issues and litigants before it.[26]

The Seventh Circuit also ignored further language in Rule 3(c), which provides that

> [i]n a class action, whether or not the class has been certified, it is sufficient for the notice to name one person qualified to bring the appeal as the representative of the class.

Fed. R. App. P. 3(c). This Court has itself held that Rule 3(c) permits Federal Rule of Civil Procedure 23 class members to appeal if the named plaintiff chooses not to do so. *United Airlines, Inc. v. McDonald*, 432 U.S. 385 (1977). Intervention is nowhere discussed in the Rule as a prerequisite to such appeals.

Finally, there is no indication that Rule 3(c)'s drafters ever intended it to preclude any nonparty appeals. To the

[25] In fact, section 1291 never mentions the words "party" or "parties" anywhere in its text. *See* Pet. App. 22a.

[26] "**(c) Content of the Notice of Appeal.**—A notice of appeal must specify the party or parties taking the appeal by naming each appellant in either the caption or the body of the notice of appeal. An attorney representing more than one party may fulfill this requirement by describing those parties with such terms as 'all plaintiffs,' 'the defendants,' 'the plaintiffs A, B, et al.,' or 'all defendants except X.' . . ." Fed. R. App. P. 3(c).

contrary, the 1967 Advisory Committee Notes indicate that the Rule "merely restate[s], in modified form, provisions now found in the civil and criminal rules . . . and decisions under the present rules which *dispense with literal compliance in cases in which it cannot fairly be exacted should control interpretation of these rules.*" 28 U.S.C. App. at 589 (emphasis added). The 1979 Advisory Committee Notes reemphasize the same point. *Id.* at 590 ("so long as the function of notice is met by the filing of a paper indicating an intention to appeal, the substance of the rule has been complied with"). In all events, contrary to the Seventh Circuit's opinion, a nonparty shareholder *can* strictly comply with the Rule's language simply by "specify[ing]" that no party is taking the appeal, and "naming each [nonparty] appellant in either the caption or the body of the notice of appeal."

II. THE SEVENTH CIRCUIT'S DECISION TO APPLY ITS RULING RETROACTIVELY CREATES ANOTHER CIRCUIT SPLIT, RAISES SIGNIFICANT QUESTIONS OF FEDERAL LAW, AND IS BASED ON A MISTAKEN PREMISE THAT WRONGLY INSULATES FROM APPELLATE SCRUTINY A PLAINLY COLLUSIVE SETTLEMENT IN ONE OF THE MOST SIGNIFICANT SHAREHOLDER DERIVATIVE SUITS

In *Harper v. Virginia Department of Taxation*, 509 U.S. 86 (1993), Chief Justice Rehnquist and Justice O'Connor commented that "[t]his Court's retroactivity jurisprudence has become somewhat chaotic in recent years." *Id.* at 113 (O'Connor, J., & Rehnquist, C.J., dissenting). This case raises a question arising from the Court's "somewhat chaotic" retroactivity jurisprudence that has split the courts of appeals. It is a question, as well, that the Seventh Circuit wrongly resolved in a manner that permanently insulates from appellate scrutiny a derivative settlement affecting millions of shareholders nationwide in an egregious case of criminal corporate behavior. All of these factors further compel this Court's review.

A. In the decision below, the Seventh Circuit took the position that *Firestone Tire & Rubber Co. v. Risjord*, 449 U.S. at 379, and its progeny forbid courts from giving purely prospective effect to any new rule "concern[ing] jurisdiction." Pet. App. 8a-9a. Accordingly, the court applied its new rule retroactively against petitioners, dismissing their appeal on the ground that they had not complied with the court's newly formulated intervention requirement. The court did so after acknowledging that petitioners had fully complied with settled Seventh Circuit appellate procedures at the time they appealed, and that retroactive application meant they would *never* be able to obtain appellate review of the ADM settlement. *Id.* at 7a-10a.

Judge Easterbrook noted that the panel's holding is in direct conflict with the Ninth Circuit's recent *en banc* decision in *George v. Camacho*, 119 F.3d 1393. Pet. App. 10a (conceding "disagree[ment] with *George*").[27] Like petitioners here, the appellant in *George* had relied on settled circuit authority (namely, precedent holding that litigants in the Northern Mariana Islands are afforded a seven-day extension for filing notices of appeal). 119 F.3d at 1395-96. As here, the Ninth Circuit concluded that its prior holding was erroneous. *Id.* But, unlike here, the Ninth Circuit refused to apply its new jurisdictional ruling retroactively to an appellant who had faithfully followed existing circuit law at the time of her appeal. *Id.*

The Ninth Circuit considered *Firestone* but, unlike the Seventh Circuit, found nothing in it mandating retroactivity:

> What underlay the Court's decision in *Firestone* was the need to ensure that litigants would not engage in piecemeal litigation, clogging the circuit courts with interlocutory appeals. . . . Applying the rule retroactively clearly advanced that objective by postponing consideration of pending interlocutory appeals until

[27] The majority in *George* included Chief Judge Hug and Judges Browning, Fletcher, Pregerson, Reinhardt, Thompson, and Hawkins.

> after final judgment. There was thus no question in *Firestone* of forfeiting anyone's right to appeal permanently. The circumstances here are entirely different.

Id. at 1397-98. The majority was joined in this view by two dissenters, Judges Kozinski and O'Scannlain, who agreed that "[a] fair and sensible solution would be to give the benefit of the error to anyone who actually relied on it. . . . This would balance appellees' interest in finality with the reliance interest of those appellants who followed our misstatement in [the prior case granting a seven-day extension]." *Id.* at 1410.[28]

The Tenth Circuit in *Pettyjohn v. Shalala*, 23 F.3d 1572 (1994), has also held, in conflict with the decision here, that nothing in *Firestone* requires retroactivity in jurisdictional disputes where appellants would be barred from ever raising their issues before a court of appeals. *Id.* at 1575. Before this case, moreover, the Seventh Circuit had taken the same position as the Ninth and Tenth Circuits. Pet. App. 10a ("overrul[ing] *Snyder*," which had held that *Firestone* simply does "not address the issue of whether an appellate court must dismiss the appeal where a party who relies on a jurisdictional ruling is, under a subsequent decision, foreclosed from ever raising his issues in the appellate court," 736 F.2d at 415).

B. Though the courts of appeals sharply differ over *Firestone*'s scope, they agree that the issue dividing them raises important questions for the administration of justice and access to the federal courts.

If the Ninth and Tenth Circuits (and the Seventh Circuit in *Snyder*) are correct and courts may apply jurisdictional rulings only prospectively, the Seventh Circuit has set itself on a course that will systematically deny

[28] These dissenters simply took issue with whether the appellant in *George* had in fact relied on the court's prior decision or had simply been neglectful. 119 F.3d at 1410. There is no question in this case, and no suggestion in the record, that petitioners have acted in any neglectful fashion.

substantive review to valid appeals; litigants relying on settled law overturned in their own cases will be barred from ever arguing their issues on appeal. This result is obviously inequitable to an entire class of litigants, and it directly undercuts the judiciary's strong interest in promoting reliance on settled law. *George*, 119 F.3d at 1397 ("The consequence of such a holding would be that litigants who complied with our rules . . . would lose their rights to appeal, . . . a result that would appear to be unconscionable to most reasoning persons whether learned in the law or not."); *Snyder*, 736 F.2d at 415 (such a holding would be "obviously unfair"; " 'it would be inequitable for an appellate court to decline to hear the appeal' ") (citation omitted).

This result also creates a bizarre incentive for litigants to file every conceivable paper and motion—even those already expressly ruled wasteful and superfluous—solely as an insurance policy against a possible change in law. *George*, 119 F.3d at 1404 ("Rules are intended to provide certainty and to guide parties' actions. Making a [jurisdictional] rule . . . retroactive [in all cases] is inconsistent with both of these objectives.") (footnote omitted).

By contrast, if the Seventh Circuit is right and *Firestone* mandates retroactive application of all new jurisdictional rules, the Ninth Circuit has lawlessly arrogated power to hear appeals over which it has no valid jurisdiction. Indeed, the Seventh Circuit below chided the Ninth Circuit on precisely these grounds.[29]

C. As a result of the Seventh Circuit's decision, lawyers will keep all of the meager $8 million ADM settlement; the company and its millions of shareholders will receive no meaningful reforms and not one dime from

[29] "The proposition that 'a court may not in any case, even in the interest of justice, extend its jurisdiction where none exists' requires us to overrule *Snyder* and disagree with *George*. Jurisdiction means adjudicatory power. Equitable considerations are altogether irrelevant when a court lacks adjudicatory power." Pet. App. 10a (citation omitted).

fiduciaries guilty of gross abuses of trust. All of this will take place, moreover, without any appellate review and as a result of a clear error of law.

The Seventh Circuit rested its decision on the premise that, once a court has determined that it lacks jurisdiction, it is powerless to reach the merits of the case no matter how inequitable that may be. "[A] court may not in any case, even in the interest of justice, extend its jurisdiction where none exists." Pet. App. 10a (internal quotation marks omitted).

That premise, however, is unsupported. The Seventh Circuit plainly *did* have "adjudicatory power" to hear petitioners' appeal. The panel never suggested that it lacked statutory or constitutional authority to entertain nonparty shareholder appeals. Nothing in the language of 28 U.S.C. § 1291 or practice under that section even hints that appeals are limited to formal parties. *See* Pet. App. 22a (text of section 1291); notes 21-24, *supra* (documenting longstanding practice of permitting nonparty appeals in federal appellate courts). Nothing in the Federal Rules of Appellate Procedure precludes nonparty shareholder appeals. *See* Point I.C, *supra*. And it is beyond dispute that petitioners, among ADM's largest shareholders, have standing under Article III.[30]

Given the undisputed *presence* of constitutional and statutory "adjudicatory authority," the Seventh Circuit's ruling below can most generously be described as a *prudential* decision. It reflects a policy decision akin to the judicially created prudential standing doctrine,[31] not any

[30] Judge Easterbrook himself conceded that petitioners have constitutional standing in the course of criticizing the Third Circuit's decision in *Bell Atlantic*. *See* note 19, *supra* (quoting Pet. App. 6a-7a).

[31] *See, e.g., Bennett v. Spear*, 117 S. Ct. 1154, 1161 (1997) ("In addition to the immutable requirements of Article III, 'the federal judiciary has also adhered to a set of prudential principles that bear on the question of standing.' Like their constitutional counterparts, these 'judicially self-imposed limits on the exercise of federal juris-

outside constraint on the courts' authority. There was no reason why the court of appeals could not have at least *considered* whether to apply this purely prudential rule prospectively. The court's suggestion that it lacked "adjudicatory power" to weigh such an option lacks any basis in law or common sense.

In any event, even if the court of appeals' "jurisdictional" ruling had affected the power of the court under statutory or constitutional law, its decision still could not be squared with *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982). There the Court held Congress's grant of jurisdiction to bankruptcy courts *unconstitutional*. Nonetheless, the Court applied *Chevron Oil Co. v. Huson*, 404 U.S. 97 (1971). The Court concluded that, because its ruling "could produce substantial inequitable results," *id.* at 106-07, it should apply its decision only prospectively; the bankruptcy courts—though determined to lack any constitutional power—were thus allowed to retain cases already pending before them. 458 U.S. at 88-89 (plurality opinion); *id.* at 91-92 (Rehnquist, J., concurring in the judgment). If the bankruptcy courts could properly hear pending cases over which they had no *constitutional* authority, the Seventh Circuit's conclusion that it is "powerless" to apply *Chevron Oil*'s balancing test is hardly convincing. The Seventh Circuit did not address *Northern Pipeline* in its opinion.[32]

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diction' are 'founded in concern about the proper—and properly limited—role of the courts in a democratic society,' but unlike their constitutional counterparts, they can be modified or abrogated by Congress.") (citations omitted); *Allen v. Wright*, 468 U.S. 737, 750-51 (1984) (same).

[32] The Seventh Circuit also suggested that *Chevron Oil*, 404 U.S. 97, had itself been "overruled" by *Harper*, 509 U.S. 86, and *James B. Beam Distilling Co. v. Georgia*, 501 U.S. 529 (1991). Pet. App. 8a. But this is simply not so. The splintered decisions in *Harper* and *Beam* held only that when a court decides to apply a new rule of law retroactively to the parties before it, it must also apply that same rule retroactively to all cases still open on direct review; selectively applying the new rule only to litigants at hand while retaining the old rule for all other pending cases is not permitted. Nothing in these decisions "overruled" a court's ability to consider under *Chevron Oil* whether to apply a new rule of civil law only prospectively.

The Seventh Circuit rested instead on one of *Firestone*'s recent progeny, *Budinich v. Becton Dickinson & Co.*, 486 U.S. at 203. There the Court did apply a new rule of law retroactively even though doing so meant, as here, "that the losing party could never appeal." Pet. App. 9a. Because the Supreme Court there applied a jurisdictional ruling retroactively in the face of potentially inequitable consequences, the court of appeals reasoned that "*Budinich* . . . washes away the distinction we drew in *Snyder*" and any suggestion that the court of appeals remains empowered to consider prospective decisionmaking in cases "concern[ing] jurisdiction." *Id.*

The Seventh Circuit's reliance on *Budinich* is mistaken for three reasons. *First*, and most significantly, the Court in *Budinich* was called upon to render a decision concerning the court of appeals' *statutory* authority under 28 U.S.C. § 1291.[33] Its decision to apply its ruling concerning the courts' *statutory* jurisdiction retroactively has no bearing on the question whether the panel below was bound to apply its *prudential* decision retroactively.

Second, because *Budinich* announced no new rule of law, it was not eligible for purely prospective application. *See Harper*, 509 U.S. at 111 (Kennedy, J., concurring) (a decision cannot be made nonretroactive unless it "overrul[es] clear past precedent on which litigants may have relied" or "decid[es] an issue of first impression whose resolution was not clearly foreshadowed"). Instead, as the Ninth Circuit has pointed out, *Budinich* merely reaffirmed what "should have been apparent from the Court's previous decisions"—namely that a judgment is final and appealable under section 1291 after adjudication on the

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[33] 486 U.S. at 199 ("The question before us . . . is whether a decision on the merits is a 'final decision' as a matter of federal law under § 1291 when the recoverability or amount of attorney's fees for the litigation remains to be determined.").

merits and does not await determination of attorneys' fees. *George*, 119 F.3d at 1398; *id.* (*Budinich* "did not change the applicable law"; it "did not conflict with or overrule any previously established law; nor did it subject Budinich to a rule that was different from the rule in effect at the time he acted").

Third, even supposing *Budinich* had effected a change in law, the petitioner in *Budinich* relied on no existing authority and ignored multiple warning signals from the Supreme Court that her position was wrong. Whatever "inequitable results" under a *Chevron Oil* analysis might conceivably flow from retroactive application against the petitioner in *Budinich* simply cannot be compared to those in this case. *See George*, 119 F.3d at 1398 (applying rule prospectively after *Chevron Oil* test and distinguishing *Budinich* because, as here, "the new rule [in *Budinich*] did not wipe out any rights [the petitioner] had established under a former version of the rule").[34]

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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[34] *See also id.* at 1410 (Kozinski & O'Scannlain, JJ., dissenting) ("A fair and sensible solution would be to give the benefit of the error to anyone who actually relied on it. . . . This would balance appellees' interest in finality with the reliance interest of those appellants who followed our misstatement in [the prior case].").

APPENDICES

APPENDIX A

UNITED STATES COURT OF APPEALS
SEVENTH CIRCUIT

No. 97-2829

PAUL FELZEN, Trustee of Louise Laskin Trust—1991, and SANDRA ESNER,
Plaintiffs-Appellees,

v.

DWAYNE O. ANDREAS, *et al.*,
Defendants,

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM and FLORIDA STATE BOARD OF ADMINISTRATION,
Objectors-Appellants.

Submitted Sept. 19, 1997
Decided Jan. 21, 1998

Before POSNER, Chief Judge, and FLAUM and EASTERBROOK, Circuit Judges.

EASTERBROOK, Circuit Judge.

"The rule that only parties to a lawsuit, or those that properly become parties, may appeal an adverse judgment, is well settled. The Court of Appeals suggested that there may be exceptions to this general rule, primarily 'when the nonparty has an interest that is affected by the trial court's judgment.' We think the better practice is for such a non-

party to seek intervention for purposes of appeal; denials of such motions are, of course, appealable." *Marino v. Ortiz*, 484 U.S. 301, 304, 108 S.Ct. 586, 587-88, 98 L.Ed.2d 629 (1988) (citations omitted). With these words the Supreme Court held that a person adversely affected by the settlement of a class action may appeal from the consent decree based on that settlement only if he has intervened as a party. See also Fed. R.App. P. 3(c): "A notice of appeal must specify the *party or parties* taking the appeal by naming each appellant in either the caption or the body of the notice of appeal." (Emphasis added.) Following *Marino* we held that a class member in an action under Fed. R. Civ. P. 23 who has not become a party may not appeal from an order granting summary judgment to the defendant. *In re Brand Name Prescription Drugs Antitrust Litigation*, 115 F.3d 456 (7th Cir.1997). Today we consider another proposed exception to the rule stated in *Marino*.

Courts have disagreed for several decades about whether class members (and shareholders, their counterparts in derivative actions under Rule 23.1) must intervene as parties in order to appeal from adverse decisions. See Comment, *The Appealability of Class Action Settlements by Unnamed Parties*, 60 U.Chi.L.Rev. 933 (1993). Until *Marino* this circuit permitted class members and stockholders to appeal, whether or not they had intervened, provided they had informed the district court of their objections to the decision that disadvantaged them. See *Research Corp. v. Asgrow Seed Co.*, 425 F.2d 1059 (7th Cir.1970) (class action); *Tryforos v. Icarian Development Co.*, 518 F.2d 1258, 1263 n. 22 (7th Cir.1975) (shareholders' derivative suit). We held in *Brand Name Prescription Drugs* that in light of *Marino* and *In re VMS Limited Partnership Securities Litigation*, 976 F.2d 362 (7th Cir.1992), *Asgrow Seed* is no longer authoritative. 115 F.3d at 458. But two shareholders who have appealed from the district court's approval of a settlement in this

derivative action ask us to apply *Tryforos* notwithstanding intervening precedent and the language of Rule 3(c).

Tryforos did not analyze the question now before us—whether shareholders who are not parties to a Rule 23.1 action nonetheless may appeal—but stated that their right to so do is "clear". Footnote 22 in *Tryforos* cites one case from the 1940s that permits such appeals, but that opinion did not give reasons. (*Tryforos* also cites one district court opinion from the 1960s, an odd reference for a rule of appellate jurisdiction.) An unexplained practice does not offer shelter from a later opinion of the Supreme Court holding that only parties may appeal, and withdrawing from the appellate courts any exception-making power. The two shareholder-appellants offer a number of arguments in support of appeal without intervention that boil down to a claim that erroneous decisions should be reversed, but arguments of this stripe do not justify omitting the step of intervening as a party. A court of appeals is not an ombudsman. Suppose the settlement of a derivative action induces the corporation to fire its CEO, or to curtail its purchases of fax machines, or to choose a different law firm. The affected employees, vendors, and lawyers could not appeal just because they believed the settlement improvident or the judge's action in approving it legally erroneous. Only parties may appeal. So too with shareholders, who have no more right to speak for the firm or control its litigation decisions than bondholders or banks or landlords, all of whom have contractual interests that may be affected by litigation. It may be, as appellants stress, that some district judges would not be receptive to attempts to intervene for the purpose of appeal, but the Supreme Court spoke to this in *Marino* when observing that a denial of a motion to intervene is itself appealable.

According to appellants, *Brand Name Prescription Drugs* did not actually jettison the approach of *Asgrow Seed* even for class actions. The question at issue in *Brand Name Prescription Drugs* was whether class mem-

bers (other than the named representatives) could appeal from an order granting summary judgment, while *Asgrow Seed* and today's case involve an appeal from an order approving a settlement. *VMS Limited Partnership*, while dismissing the appeal at hand, remarked in a footnote that the decision did not disturb *Asgrow Seed*. 976 F.2d at 368 n. 8. That is technically so; neither *VMS Limited Partnership* nor *Brand Name Prescription Drugs* involved an appeal from an order approving a settlement. But the distinction is inconsequential for purposes of Rule 3(c), the rationale of *Marino*, and the rationale of *Brand Name Prescription Drugs*: that the court should not "fragment the control of the class action" (115 F.3d at 457) by allowing class members to usurp the role of the class representative without persuading the district judge that the representative is unfit or unfaithful, or that subclasses should be created. See also *Shults v. Champion International Corp.*, 35 F.3d 1056, 1060-61 (6th Cir.1994); *Gottlieb v. Wiles*, 11 F.3d 1004, 1010-12 (10th Cir. 1993). Lest doubt linger, we now formally overrule *Asgrow Seed* and any other case in this circuit (including *Armstrong v. Board of School Directors*, 616 F.2d 305, 327-28 (7th Cir.1980), and *Patterson v. Stovall*, 528 F.2d 108, 109 n. 1 (7th Cir.1976)) that permits non-parties to appeal from a decision of any kind in a class action.

Well, then, is a shareholders' derivative action under Rule 23.1 different from a class action under Rule 23 in a way that permits appeal by nonparties? Not so far as Rule 3(c) or *Marino* is concerned. Although there are differences between class actions and derivative suits, these cut against the appellants' position. All class members are identical in entitlement to litigate; which injured persons become the representatives, and which the "mere" class members, is to a degree fortuitous and to a degree dependent on the entrepreneurial activity of the class counsel. It is the fact that each class member has a real grievance with the defendant that sets up at least an equitable argument for a class member who wants to appeal. But in a

shareholders' derivative action, the individual investor is not an injured party and is not entitled to litigate. A derivative suit is brought by an investor in the corporation's (not the investor's) right to recover for injury to the corporation. *Frank v. Hadesman & Frank, Inc.*, 83 F.3d 158 (7th Cir.1996); *Kagan v. Edison Brothers Stores, Inc.*, 907 F.2d 690 (7th Cir.1990). The corporation obtains the damages; the investor-plaintiffs just get the ball rolling after the fashion of a *qui tam* action. Only when the corporation's board defaults in its duty to protect the interests of the investors is this step permitted, and even then many states permit the board to regain control of the litigation following a special investigation. See *Kamen v. Kemper Financial Services, Inc.*, 500 U.S. 90, 111 S.Ct. 1711, 114 L.Ed.2d 152 (1991); American Law Institute, *Principles of Corporate Governance: Analysis and Recommendations* §§ 7.01, 7.03, 7.05 (1992). If in the course of managing or settling derivative litigation investors receive new injury, they do so only because the corporation becomes worse off—but loss to the corporation does not permit stockholders to sue directly. See *Mid-State Fertilizer Co. v. Exchange National Bank*, 877 F.2d 1333 (7th Cir.1989). Once again the corporation holds the legal claim, and it acts through the board of directors. Stockholders may *replace* the board if dissatisfied with its performance, but they may not *displace* the board in litigation. So it cannot be surprising that stockholders other than the named plaintiffs are not treated as parties in derivative litigation—their citizenship is ignored when determining diversity, see *Smith v. Sperling*, 354 U.S. 91, 77 S.Ct. 1112, 1 L.Ed.2d 1205 (1957), and they are not allowed to opt out. Corporate management may affect the interests of stockholders without notifying them or obtaining their consent; by investing in stock, they placed their funds at the management's disposal and obtained, in exchange, the right to choose future managers. Shareholders have no more the attributes of parties when managers settle derivative litigation than when managers settle antitrust

litigation. (This particular derivative suit arose out of claims that managers of Archer Daniels Midland Co. conspired with rival sellers and thus exposed the firm to criminal and treble-damages liability for conspiracy in restraint of trade.)

Rule 23.1 provides for notice to shareholders only in the event of dismissal or settlement, so that other investors may contest the faithfulness or honesty of the self-appointed plaintiffs; we do not doubt that this monitoring is often useful and that intervention to facilitate an appeal could be justified. Many thoughtful students of the subject conclude, with empirical support, that derivative actions do little to promote sound management and often hurt the firm by diverting the managers' time from running the business while diverting the firm's resources to the plaintiffs' lawyers without providing a corresponding benefit. Janet Cooper Alexander, *Do the Merits Matter? A Study of Settlements in Securities Class Actions*, 43 Stan. L.Rev. 497 (1991); Reinier Kraakman, Hyun Park & Steven Shavell, *When are Shareholder Suits in Shareholder Interests?*, 82 Geo. L.J. 1733 (1994); Roberta Romano, *The Shareholder Suit: Litigation Without Foundation?*, 7 J.L. Econ. & Org. 55 (1991); Mark L. Cross, Wallace N. Davidson & John H. Thornton, *The Impact of Directors' and Officers' Liability Suits on Firm Value*, 56 J. Risk & Insurance 128 (1989); Daniel R. Fischel & Michael Bradley, *The Role of Liability Rules and the Derivative Suit in Corporate Law: A Theoretical and Empirical Analysis*, 71 Cornell L.Rev. 261 (1986). The two shareholder-appellants in this case believe that the modest settlement, half of which will be paid to counsel, exemplifies this problem. Their failure to become parties prevents us from considering this contention, for the possibility that a district court's judgment is erroneous does not dispense with the need for an appeal by a party.

One court of appeals has held, despite *Marino*, that a shareholder need not become a party in order to appeal

from the final decision in derivative litigation. *Bell Atlantic Corp. v. Bolger*, 2 F.3d 1304, 1307-10 (3d Cir.1993). The third circuit conceived of the question as whether the shareholder has standing, which is misleading. Standing means injury in fact, and a reduction in the market price of one's stock is injury. Parties are a subset of injured persons. Equating injury with party status is exactly the approach disapproved by *Marino*. The third circuit thought that shareholders in derivative actions should be treated like class members in class actions, and it permitted the shareholders to appeal because it permits class members to appeal. 2 F.3d at 1309-10; see also *Carlough v. Amchem Products, Inc.*, 5 F.3d 707, 714 (3d Cir. 1993). One does not follow from the other; for reasons we have discussed, shareholders have the weaker claim. But in this circuit, which requires class members to intervene if they want to appeal, similar treatment of shareholders is ordained. We overrule *Tryforos* to the extent it permits non-party shareholders to appeal in actions under Rule 23.1, and we disagree with the conclusion of *Bell Atlantic*.

Appellants tell us that they relied on *Asgrow Seed* and *Tryforos* when deciding not to intervene as parties and implicitly ask us to defer the effect of any decision to overrule their holdings. But "[a] court lacks discretion to consider the merits of a case over which it is without jurisdiction, and thus, by definition, a jurisdictional ruling may never be made prospective only." *Firestone Tire & Rubber Co. v. Risjord*, 449 U.S. 368, 379, 101 S.Ct. 669, 676, 66 L.Ed.2d 571 (1981).

Notwithstanding *Firestone*, the ninth circuit recently refused, on equitable grounds, to apply to pending cases a decision overruling a jurisdictional precedent. *George v. Camacho*, 119 F.3d 1393 (9th Cir.1997) (en banc). *George* stated that despite the sweep of its language *Firestone* should be confined to situations in which the disappointed appellant has some later opportunity to present

the claims to the court of appeals. A panel of this court reached the same conclusion in *Snyder v. Smith*, 736 F.2d 409, 415 (7th Cir.1984): "In [*Firestone*], the court of appeals held that an order denying a motion to disqualify counsel was not appealable prior to final judgment but, because its holding was contrary to precedent, it determined the merits of the order. The Supreme Court held that when an appellate court finds an order interlocutory and nonappealable, the court must dismiss the appeal. The Court did not address the issue of whether an appellate court must dismiss the appeal where a party who relies on a jurisdictional ruling is, under a subsequent decision, foreclosed from ever raising his issues in the appellate court. Thus, *Firestone* does not require this court to dismiss the appeal." When deciding whether to dismiss an appeal in light of new precedent, we concluded in *Snyder*, a court of appeals should look not to *Firestone* but to *Chevron Oil Co. v. Huson*, 404 U.S. 97, 92 S.Ct. 349, 30 L.Ed.2d 296 (1971), which gives a dominant role to equitable interests such as reliance on precedent.

Cases decided by the Supreme Court since *Snyder* require us to proceed differently. *Chevron* has been overruled. Harper v. Virginia Department of Taxation, 509 U.S. 86, 113 S.Ct. 2510, 125 L.Ed.2d 74 (1993); *James B. Beam Distilling Co. v. Georgia*, 501 U.S. 529, 111 S.Ct. 2439, 115 L.Ed.2d 481 (1991). The second court no longer considers whether application of the new rule would be inequitable or undermine reliance interests. Instead, when a court "applies a rule of federal law to the parties before it, that rule is the controlling interpretation of federal law and must be given full retroactive effect in all cases still open on direct review and as to all events, regardless of whether such events predate or postdate [the] announcement of the rule." *Harper*, 509 U.S. at 97, 113 S.Ct. at 2517. This language holds out the option of announcing a rule with wholly prospective force, inapplicable to the parties in the case that announces the rule. But a second line of cases, including *Firestone*, withholds

the option of complete prospectivity when the rule concerns jurisdiction. Seven years after *Firestone* (and four years after *Snyder*) a litigant asked the Supreme Court to make a ruling prospective in order to prevent a "significant change in the law" from knocking out appellate jurisdiction. The Court declined. *Budinich v. Becton Dickinson & Co.*, 486 U.S. 196, 203, 108 S.Ct. 1717, 1722, 100 L.Ed.2d 178 (1988) (citing and quoting from *Firestone*). *Budinich*, like *Snyder*, *George*, and the case now at hand, involved an appeal from a final judgment; the holding in *Budinich* meant that the losing party could never appeal, a conclusion that washes away the distinction we drew in *Snyder*. Later the same Term, the Court reiterated the point in language equally pertinent today:

> Our agreement with the [court of appeals'] conclusion that it lacked jurisdiction, compels us to disapprove of its decision to reach the merits anyway "in the interest of justice." 822 F.2d at 1559. "Courts created by statute can have no jurisdiction but such as the statute confers." *Sheldon v. Sill*, 49 U.S. (8 How.) 441, 449, 12 L.Ed. 1147 (1850). See also *Firestone Tire & Rubber Co. v. Risjord*, 449 U.S. 368, 379-380, 101 S.Ct. 669, 676, 66 L.Ed.2d 571 (1981). . . . The age-old rule that a court may not in any case, even in the interest of justice, extend its jurisdiction where none exists has always worked injustice in particular cases. Parties often spend years litigating claims only to learn that their efforts and expense were wasted in a court that lacked jurisdiction. . . . Such situations inhere in the very nature of jurisdictional lines, for as our cases aptly illustrate, few jurisdictional lines can be so finely drawn as to leave no room for disagreement on close cases. See, *e.g.*, *K Mart Corp. v. Cartier, Inc.*, 485 U.S. 176, 108 S.Ct. 950, 99 L.Ed.2d 151 (1988); *United States v. Hohri*, 482 U.S. 64, 107 S.Ct. 2246, 96 L.Ed.2d 51 (1987).

Christianson v. Colt Industries Operating Corp., 486 U.S. 800, 818, 108 S.Ct. 2166, 2178, 100 L.Ed.2d 811 (1988). The proposition that "a court may not in any case, even in the interest of justice, extend its jurisdiction where none exists" requires us to overrule *Snyder* and disagree with *George*. Jurisdiction means adjudicatory power. Equitable considerations are altogether irrelevant when a court lacks adjudicatory power. Cf. *Landgraf v. USI Film Products*, 511 U.S. 244, 274, 114 S.Ct. 1483, 1501-02, 128 L.Ed.2d 229 (1994) (pointing out that statutes repealing grants of jurisdiction apply to pending cases, notwithstanding reliance interests); *Yang v. INS*, 109 F.3d 1185 (7th Cir.1997). If the shareholders had appealed to the House of Lords, that tribunal would have dismissed the appeal out of hand. An appeal by nonparties is no different in effect.

Because this opinion overrules some of our decisions and creates a conflict among the circuits, it was circulated before release to all judges in active service. See Circuit Rule 40(e). No judge favored hearing the case en banc.

The appeal is dismissed for want of jurisdiction.

APPENDIX B

[Filed July 7, 1997]

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF ILLINOIS

No. 95-2279

PAUL FELZEN, TRUSTEE OF LOUISE LASKIN TRUST—1991 AND SANDRA ESNER,

Plaintiff,

vs.

DWAYNE O. ANDREAS, RALPH BRUCE, JOHN H. DANIELS, HOWARD G. BUFFETT, LOWELL W. ANDREAS, JAMES R. RANDALL, MICHAEL D. ANDREAS, H.D. HALE, O. GLENN WEBB, MARTIN ANDREAS, MARGARETTA ROCKEFELLER, F. ROSS JOHNSON, RAY A. GOLDBERG, JOHN K. VANIER, SHREVE M. ARCHER, JR., M. BRIAN MULRONEY, AND ROBERT S. STRAUSS,

Defendant.

and

ARCHER DANIELS MIDLAND COMPANY,
a Delaware corporation,

Nominal Defendant.

FINAL JUDGMENT AND ORDER OF DISMISSAL

This matter having come before the court for hearing, pursuant to the order of this court, dated May 30, 1997, on the application of the parties for approval of the settlement set forth in the stipulation of settlement, dated as of May 29, 1997 (the "stipulation") and due and adequate notice having been given to the shareholders of Archer

Daniels Midland Company, and the court having considered all papers filed and proceedings had herein and otherwise being fully informed in the premises and good cause appearing therefore, IT IS HEREBY ORDERED, ADJUDGED AND DECREED that:

1. This court has jurisdiction over the subject matter of this action and over all parties to this action.

2. The definitions of terms in the stipulation are incorporated herein as though fully set forth in this judgment.

3. The notice given to the shareholders of Archer Daniels Midland Company, including the individual notice to current shareholders who could be identified through reasonable effort, of the settlement and other matters set forth in the stipulation was the best notice practicable under the circumstances. The notice provided due and adequate notice of the proceedings and of the matters set forth therein, including the proposed settlement, to all persons entitled to notice, and the notice fully satisfied the requirements of Rule 23.1 of the Federal Rules of Civil Procedure and the requirements of due process.

4. Pursuant to Rule 23.1 of the Federal Rules of Civil Procedure, this court hereby approves the settlement set forth in the stipulation and finds that the settlement is, in all respects, fair, reasonable and adequate to Archer Daniels Midland company ("ADM") and its shareholders.

5. The court hereby dismisses this action against the company (as defined in the stipulation) and the individual defendants (as defined in the stipulation) with prejudice and without costs (except as otherwise provided in the stipulation).

6. The court hereby dismisses without prejudice all claims in this action directed against Michael D. Andreas (as defined in the stipulation), which claims shall become the sole property of the company.

7. Upon the effective date, each and every settled claim is and shall be deemed to be conclusively released. "Settled claims" shall mean any and all causes of action, suits, demands, claims, matters and issues, whether known or unknown, which have been, could have been, or in the future might be asserted, advanced or alleged in this action or in the action pending in the Delaware Court of Chancery captioned *In re Archer Daniels Midland Company Derivative Litigation*, Consolidated No. 14403 (the Delaware Action) or in any court or arbitration proceeding (including, without limitation, any claims, actions or demands arising under any federal or state law relating to alleged fraud, breach of any duty, negligence, recklessness, violations of federal or state securities laws, violations of federal or state antitrust laws or otherwise) by or on behalf of the company (as defined in the stipulation), by any shareholder of said company derivatively on its behalf, or by any named plaintiff in this action or the Delaware Action (as defined in the stipulation) on their own behalf or on behalf of any record or beneficial holder of the stock of the company (as defined in the stipulation), whether individual, class, derivative, representative, legal, equitable, or any other type in any other capacity, which claims have arisen, could have arisen, arise now or hereafter arise out of, or relate in any manner to the allegations, transactions, matters or occurrences, representations, acts or omissions, or any series thereof, involved, set forth, referred to, or related to any of the pleadings in this action or the Delaware action (as defined in the stipulation) against the company (as defined in the stipulation) and/or any of the individual defendants (as defined in the stipulation), provided, however, that settled claims shall not include any claims which the company may have against Andreas (as defined in the stipulation) or Wilson (as defined in the stipulation), which claims shall be reserved to the company in the sole discretion of the company's board of directors.

8. Upon the effective date, the company (as defined in the stipulation) and each of the director defendants (as

defined in the stipulation) shall be deemed to have, and by operation of this judgment shall have, fully, finally, and forever released, relinquished and discharged the plaintiffs and counsel to the plaintiffs, each only in his or her capacity as such, from all claims arising out of, relating to, or in connection with the institution, prosecution, assertion or resolution of this action or the settled claims.

9. Upon the effective date, ADM shall be deemed to have, and by operation of this judgment shall have, fully, finally and forever discharged all settled claims. Any claims which ADM has against the excluded persons, or which ADM may have against Andreas or Wilson are expressly reserved to the company in the sole discretion of the company's board of directors.

10. Upon the effective date, ADM shall be deemed to have, and by operation of this judgment shall have, fully, finally, and forever discharged any claims which it may have against the individual defendants for reimbursement of any costs or fees advanced for them (or on their behalf) for defense of the settled claims.

11. Without affecting the finality of this judgment in any way, this court retains continuing jurisdiction over (a) implementation of this settlement; (b) the claims against the defendants in this action until the effective date (as defined in the stipulation) and until each and every act agreed to be performed by the parties to the stipulation shall have been performed pursuant to the stipulation; (c) all parties to this action for the purpose of enforcing and administering the stipulation and the releases contained therein; and (d) any other matter related or ancillary thereto.

12. In the event that the settlement does not become effective in accordance with the terms of the stipulation, then this judgment shall be rendered null and void and shall be vacated and, in such event, subject to Section F,

paragraph 2 of the stipulation, all orders entered and releases delivered in connection therewith shall be null and void.

ENTER this 7th day of July, 1997.

/s/ Harold A. Baker
HAROLD A. BAKER
United States District Judge

APPENDIX C

[Filed July 7, 1997]

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF ILLINOIS

No. 95-2279

PAUL FELZEN, TRUSTEE OF
LOUIS LASKIN TRUST 1991, *et al.*,
Plaintiff,

vs.

DWAYNE O. ANDREAS, *et al.*,
Defendants.

ORDER AWARDING ATTORNEYS' FEES AND REIMBURSEMENT OF EXPENSES

This matter coming to be heard before the United States District Court for the Central District of Illinois (the "district court"), on the 7th day of July, 1997, and the court having considered all papers filed herein and the proceedings conducted herein, having found the settlement of the present litigation to be fair, reasonable and adequate, and otherwise being fully informed in the premises hereof, it is hereby ordered, adjudged and decreed as follows:

1. The court finds that it has jurisdiction over the subject matter hereof, all parties hereto, and all matters relating to the present litigation.

2. All of the capitalized terms used herein shall have the same meaning as set forth in the stipulation of settlement dated May 29, 1997, (the "stipulation"), which was

filed herein on May 30, 1997, as part of an agreed motion for preliminary approval of the settlement (Dkt. #60).

3. The fees, expenses, and interest thereon, as awarded herein, shall be paid as directed herein from the settlement proceeds, and subject to the terms, conditions, and obligations of the stipulation, and in particular paragraph V.C. of said stipulation.

4. Considering: the results accomplished; the contribution of the various plaintiff attorneys; the complexity of the actions; the fee arrangements in similar litigation; a lodestar analysis; and the cap on fees and expenses negotiated between the parties plaintiff and defendant; the court hereby awards gross fees and expenses to the plaintiffs' attorneys in the amount of 49 percent of the settlement proceeds ($3,920,000.00).[1] These fees and expenses shall be divided 60 percent to the federal action or $2,352,000, and 40 percent or $1,568,000 to the Delaware actions. These awards shall include pro-rata interest earned thereon, which interest shall continue to accrue until said award from the Settlement Proceeds is paid to the attorneys representing the various plaintiffs in the federal and Delaware actions.

ENTER this 7th day of July, 1997.

/s/ Harold A. Baker
HAROLD A. BAKER
United States District Judge

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[1] *Cf. Florin v. Nationsbank of Georgia*, 34 F.3d 560, *passim* (7th Cir. 1994); *In Re Matter of Continental Illinois Securities Litigation*, 962 F.2d 566, *passim* (7th Cir. 1992). (setting fees from a common fund).

APPENDIX D

Federal Rule of Civil Procedure 23.1. **Derivative Actions by Shareholders**

In a derivative action brought by one or more shareholders or members to enforce a right of a corporation or of an unincorporated association, the corporation or association having failed to enforce a right which may properly be asserted by it, the complaint shall be verified and shall allege (1) that the plaintiff was a shareholder or member at the time of the transaction of which the plaintiff complains or that the plaintiff's share or membership thereafter devolved on the plaintiff by operation of law, and (2) that the action is not a collusive one to confer jurisdiction on a court of the United States which it would not otherwise have. The complaint shall also allege with particularity the efforts, if any, made by the plaintiff to obtain the action the plaintiff desires from the directors or comparable authority and, if necessary, from the shareholders or members, and the reasons for the plaintiff's failure to obtain the action or for not making the effort. The derivative action may not be maintained if it appears that the plaintiff does not fairly and adequately represent the interests of the shareholders or members similarly situated in enforcing the right of the corporation or association. The action shall not be dismissed or compromised without the approval of the court, and notice of the proposed dismissal or compromise shall be given to shareholders or members in such manner as the court directs.

APPENDIX E

Federal Rule of Appellate Procedure 3. **Appeal as of Right—How Taken**

(a) Filing the Notice of Appeal. An appeal permitted by law as of right from a district court to a court of appeals must be taken by filing a notice of appeal with the clerk of the district court within the time allowed by Rule 4. At the time of filing, the appellant must furnish the clerk with sufficient copies of the notice of appeal to enable the clerk to comply promptly with the requirements of subdivision (d) of this Rule 3. Failure of an appellant to take any step other than the timely filing of a notice of appeal does not affect the validity of the appeal, but is ground only for such action as the court of appeals deems appropriate, which may include dismissal of the appeal. Appeals by permission under 28 U.S.C. § 1292(b) and appeals in bankruptcy must be taken in the manner prescribed by Rule 5 and Rule 6 respectively.

(b) Joint or Consolidated Appeals. If two or more persons are entitled to appeal from a judgment or order of a district court and their interests are such as to make joinder practicable, they may file a joint notice of appeal, or may join in appeal after filing separate timely notices of appeal, and they may thereafter proceed on appeal as a single appellant. Appeals may be consolidated by order of the court of appeals upon its own motion or upon motion of a party, or by stipulation of the parties to the several appeals.

(c) Content of the Notice of Appeal.—A notice of appeal must specify the party or parties taking the appeal by naming each appellant in either the caption or the body of the notice of appeal. An attorney representing more than one party may fulfill this requirement by describing those parties with such terms as "all plaintiffs," "the defendants," "the plaintiffs A, B, et al.," or "all defendants except X." A notice of appeal filed pro se is filed on

behalf of the party signing the notice and the signer's spouse and minor children, if they are parties, unless the notice of appeal clearly indicates a contrary intent. In a class action, whether or not the class has been certified, it is sufficient for the notice to name one person qualified to bring the appeal as representative of the class. A notice of appeal also must designate the judgment, order, or part thereof appealed from, and must name the court to which the appeal is taken. An appeal will not be dismissed for informality of form or title of the notice of appeal, or for failure to name a party whose intent to appeal is otherwise clear from the notice. Form 1 in the Appendix of Forms is a suggested form for a notice of appeal.

(d) Serving the Notice of Appeal.—The clerk of the district court shall serve notice of the filing of a notice of appeal by mailing a copy to each party's counsel of record (apart from the appellant's), or, if a party is not represented by counsel, to the party's last known address. The clerk of the district court shall forthwith send a copy of the notice and of the docket entries to the clerk of the court of appeals named in the notice. The clerk of the district court shall likewise send a copy of any later docket entry in the case to the clerk of the court of appeals. When a defendant appeals in a criminal case, the clerk of the district court shall also serve a copy of the notice of appeal upon the defendant, either by personal service or by mail addressed to the defendant. The clerk shall note on each copy served the date when the notice of appeal was filed and, if the notice of appeal was filed in the manner provided in Rule 4(c) by an inmate confined in an institution, the date when the clerk received the notice of appeal. The clerk's failure to serve notice does not affect the validity of the appeal. Service is sufficient notwithstanding the death of a party or the party's counsel. The clerk shall note in the docket the names of the parties to whom the clerk mails copies, with the date of mailing.

(e) Payment of Fees.—Upon the filing of any separate or joint notice of appeal from the district court, the appellant shall pay to the clerk of the district court such fees as are established by statute, and also the docket fee prescribed by the Judicial Conference of the United States, the latter to be received by the clerk of the district court on behalf of the court of appeals.

APPENDIX F

28 U.S.C. § 1291. **Final decisions of district courts**

The courts of appeals (other than the United States Court of Appeals for the Federal Circuit) shall have jurisdiction of appeals from all final decisions of the district courts of the United States, the United States District Court for the District of the Canal Zone, the District Court of Guam, and the District Court of the Virgin Islands, except where a direct review may be had in the Supreme Court. The jurisdiction of the United States Court of Appeals for the Federal Circuit shall be limited to the jurisdiction described in sections 1292(c) and (d) and 1295 of this title.

(2)

FILED

JUN 15 1998

No. 97-1732

IN THE

Supreme Court of the United States

OCTOBER TERM, 1997

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM and FLORIDA STATE BOARD OF ADMINISTRATION,

Petitioners,

v.

PAUL FELZEN, et al.,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

BRIEF OF DIRECTORS OF ARCHER DANIELS MIDLAND COMPANY IN OPPOSITION

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33 pp

QUESTIONS PRESENTED

1. Whether a court of appeals, in a derivative action brought on behalf of a corporation, had jurisdiction to hear the appeal of nonparty shareholders from the district court's order approving settlement of the action.

2. Whether a court of appeals, when ruling that it does not have jurisdiction in a case, properly declined to make its decision prospective only.

TABLE OF CONTENTS

PAGE

QUESTIONS PRESENTED i

TABLE OF AUTHORITIES iv

STATEMENT OF THE CASE 1

REASONS FOR DENYING THE PETITION 3

I. PETITIONERS' BACKGROUND STATEMENT OF FACTS IS NOT RELEVANT TO THE LEGAL ISSUES INVOLVED HERE 4

II. PETITIONERS HAVE NOT IDENTIFIED A CONFLICT IN THE CIRCUITS CONCERNING THE RIGHT OF NONPARTY SHAREHOLDERS TO APPEAL FROM SETTLEMENT OF A DERIVATIVE SUIT 6

A. This Court's Holding in *Marino v. Ortiz* Is Determinative 6

B. The Seventh Circuit's Ruling Does Not Raise a Conflict Among the Circuits 8

1. The Purported Split of Authority 9

2. The State of the Law in the Seventh Circuit 11

3. Conclusion 12

C. The Seventh Circuit's Decision Requiring Intervention Is Consistent with Rule 23.1 and with Traditional Common Law and Federal Practice 13

1. Participation By Nonparty Shareholders 14

2. Rule 23.1 and Common Law 15

III. THE SEVENTH CIRCUIT'S DECISION TO APPLY ITS RULING RETROACTIVELY IS DICTATED BY PRECEDENT OF THIS COURT, RAISES NO CONFLICT IN THE CIRCUITS, AND CAUSES NO UNFORESEEABLE HARM TO PETITIONERS 19

CONCLUSION 26

TABLE OF AUTHORITIES

Cases PAGE(S)

Ace Heating & Plumbing Co. v. Crane Co.,
453 F.2d 30 (3d Cir. 1971) 9, 10

Allen v. Wright,
468 U.S. 737 (1984) 22, 23

Bell Atlantic Corp. v. Bolger,
2 F.3d 1304 (3d Cir. 1993) ..... *passim*

Bennett v. Spear,
520 U.S. 154 (1997) 22

Budinich v. Becton Dickinson & Co.,
486 U.S. 196 (1988) 21, 24, 25

Christianson v. Colt Indus. Operating Corp.,
486 U.S. 800 (1988) 21, 25

Farmland Dairies v. Comm'r of New York State Dep't of Agric. & Markets,
847 F.2d 1038 (2d Cir. 1988) 15

Firestone Tire & Rubber Co. v. Risjord,
449 U.S. 368 (1981) ..... *passim*

George v. Camacho,
119 F.3d 1393 (9th Cir. 1997) 21

Gottlieb v. Wiles,
11 F.3d 1004 (10th Cir. 1993) 9, 12, 13

Harper v. Virginia Dep't of Taxation,
509 U.S. 86 (1993) 19

In Re Brand Name Prescription Drugs Antitrust Litigation,
115 F.3d 456 (7th Cir. 1997) 8, 12, 19, 22

Jones v. Caddo Parish Sch. Bd.,
735 F.2d 923 (5th Cir. 1984) 15

Marino v. Ortiz,
484 U.S. 301 (1988) ..... *passim*

Northern Pipeline Construction Co. v. Marathon Pipe Line Co.,
458 U.S. 50 (1982) 23, 24

Pettyjohn v. Shalala,
23 F.3d 1572 (10th Cir. 1994) 20, 21

Ragsdale v. Turnock,
941 F.2d 501 (7th Cir. 1991),
cert. denied, 502 U.S. 1035 (1992) 15

Research Corp. v. Asgrow Seed Co.,
425 F.2d 1059 (7th Cir. 1970) 11

Rosenbaum v. MacAllister,
64 F.3d 1439 (10th Cir. 1985) 9, 12, 13

Tryforos v. Icarian Development Co.,
518 F.2d 1258 (7th Cir. 1975) 11, 12, 13

United States ex rel. Louisiana v. Jack,
244 U.S. 397 (1917) 17

Statute

28 U.S.C. § 1291 ..... 22, 24

Court Rules

Federal Rule of Appellate Procedure 3(c) 18, 19

Federal Rule of Civil Procedure 23 ..... *passim*

Federal Rule of Civil Procedure 23.1 ..... *passim*

STATEMENT OF THE CASE

Petitioners are two nonparty shareholders of Archer Daniels Midland Company ("ADM") who filed objections to a proposed settlement of this derivative action but failed to file a motion to intervene and, as a consequence, had no right to appeal from the district court order approving the settlement. Respondents filing this brief were members of the Board of Directors of ADM in 1995 who were named as defendants in the derivative suits filed in Illinois and Delaware.[1] These suits were settled in a consolidated process before the Honorable Harold A. Baker, United States District Judge for the Central District of Illinois, on July 7, 1997, when plaintiffs in all pending derivative actions appeared before Judge Baker and agreed to be bound by any settlement which the court approved. Petitioners, who hold less than one percent of the stock of ADM, objected to the proposed settlement below, which was predicated upon substantial changes to the way in which ADM governs itself and the creation of an Audit Committee of independent directors to monitor the company's compliance. Petitioners chose not to intervene below but, when the

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[1] Respondents (hereinafter referred to as the "Directors") are Dwayne O. Andreas, Lowell W. Andreas, Martin Andreas, Michael D. Andreas, Shreve M. Archer, Jr., Ralph Bruce, Howard G. Buffett, John H. Daniels, Ray A. Goldberg, H.D. Hale, F. Ross Johnson, M. Brian Mulroney, James R. Randall, Margaretta Rockefeller, Robert S. Strauss, John K. Vanier, and O. Glenn Webb. Gaylord O. Coan joined the Board of Directors after the events complained of in the action and was erroneously added to some of the suits filed in Delaware. Of the eighteen Directors named, eight are currently members of the Board.

district court overruled their objections and approved a settlement, Petitioners sought to appeal.

Plaintiffs below moved to dismiss Petitioners' appeal. The Court of Appeals for the Seventh Circuit (the "Seventh Circuit") dismissed Petitioners' appeal for the very basic reason that they were not parties to the case, and thus the Court had no jurisdiction over their appeal from approval of the settlement. In reaching this determination, the Seventh Circuit relied on law well settled not only in this Court but among the circuits. The Seventh Circuit also persuasively articulated the reasons that a shareholder is especially unqualified to appeal as a nonparty:

> . . . in a shareholders' derivative action, the individual investor is not an injured party and is not entitled to litigate. A derivative suit is brought by an investor in the corporation's (not the investor's) right to recover for injury to the corporation . . . . So it cannot be surprising that stockholders other than named plaintiffs are not treated as parties in derivative litigation—their citizenship is ignored when determining diversity . . . and they are not allowed to opt out . . . . Shareholders have no more the attributes of parties when managers settle derivative litigation than when managers settle antitrust litigation.

(Petition at 5a)

Now, having forfeited any right to appeal by failing to intervene as parties—all in defiance of ample precedent pointing the way—Petitioners seek a grant of *certiorari*. Meanwhile, ADM's directors have appointed an independent Audit Committee, consisting of directors who joined the board after the events of which plaintiffs

below complained and await resolution of Petitioners' efforts to undo the settlement before the Audit Committee takes steps to implement the settlement terms. For the reasons that follow, the Petition should be denied.

REASONS FOR DENYING THE PETITION

The Petition here stands as a model for advocacy by deception and diversion. Among other things, the Petition:

(1) unfairly conjures up from two circuit court cases, each distinguishable from the instant case, an "irreconcilable split" among the circuits;

(2) interposes a long statement of background facts and fervent complaints about the fairness of a court-approved shareholders' derivative suit, neither of which has any bearing upon the narrow and strictly legal issues involved here;

(3) confuses the essentially different natures of a class action under Rule 23 of the Federal Rules of Civil Procedure, where corporate shareholders allege injury to themselves, from a derivative suit under Rule 23.1 of the Federal Rules of Civil Procedure, where the corporation itself holds the legal claim and may receive damages;

(4) belittles this Court's holding in *Marino v. Ortiz*, 484 U.S. 301 (1988), almost to the point of denying its existence;

(5) misrepresents the state of the case law in the Seventh Circuit at the time Petitioners made their decision to forego intervention in the action below and thereby

assumed the obvious risk that they would not have a right to appeal;

(6) cites voluminous authority for sweeping statements concerning the importance of participation by nonparty shareholders in the judicial settlement process without ever acknowledging that the cited authority generally references proceedings only at the district court level; and

(7) offers numerous examples of appeals by nonparty "privies" that are "routinely permitted," even though each example involves a party over whom a court had already exercised jurisdiction.

I. PETITIONERS' BACKGROUND STATEMENT OF FACTS IS NOT RELEVANT TO THE LEGAL ISSUES INVOLVED HERE

The first indicator of the Petition's weakness is its highly charged statement of background facts, none of which is necessary for this Court's consideration of the well-defined legal issues involved here. Petitioners lay out the origins of the derivative suit in terms of FBI "raids," a criminal "probe," conspiracy with "foreign companies," "national media attention," "corporate cronyism," and "waves of negative publicity." (Petition at 4-5) Turning to the derivative suit itself, Petitioners complain that plaintiffs' counsel "did almost nothing to prosecute the case" and focused "what little energy they expended on settlement." (Petition at 6) The settlement, according to Petitioners, did not return "one dime" and "provided no material benefit to shareholders," allocating a payment "*exclusively* to pay for attorneys' fees." (Petition at 6-7; emphasis in original) This narrative, even if not discounted for distortions of rhetoric, has

nothing to do with the right of nonparty shareholders to appeal from a settlement of a derivative suit.

Petitioners' background statement is, however, instructive on two counts. First, it shows that ADM's nonparty shareholders were in fact accorded the participation in the judicial settlement review process that Petitioners regard as "a key procedural countermeasure" against derivative settlements too heavily weighted with attorneys' fees. (Petition at 14) The district court followed standard procedure in tentatively approving a settlement and inviting shareholders—whether parties or not—to show why the proposed settlement should not be finally approved. (Petition at 7) In response, the Petitioners filed written objections to the proposed corporate governance changes and appeared at a hearing where they asked the district court to reject or revise the settlement. (*Id.*)

Second, Petitioners' background statement reveals their underlying motivation for challenging the settlement and, ultimately, in making the Petition: they are members of the Council of Institutional Investors, "an association of more than one hundred corporate, public, and union pension funds . . . ." (Petition at 5) The "standards for corporate independence" which Petitioners sought to include in the settlement agreement were based on standards developed by the Council of Institutional Investors which, according to an unsupported assertion in the Petition, have been "adopted by most or many of the nation's largest companies." (Petition at 5) Petitioners objected that the governance standards in the proposed settlement, which the district court found consistent with established concepts of corporate governance, did not parrot the definitions which Petitioners

had recently published. Hence, Petitioners' participation in the proceedings derives at least in part from their interest in seeking judicial leverage to impose the pension funds' governance standards on a large company. (Petition at 7)

II. PETITIONERS HAVE NOT IDENTIFIED A CONFLICT IN THE CIRCUITS CONCERNING THE RIGHT OF NONPARTY SHAREHOLDERS TO APPEAL FROM SETTLEMENT OF A DERIVATIVE SUIT

A. This Court's Holding in Marino v. Ortiz Is Determinative

Petitioners' treatment of *Marino v. Ortiz*, *supra*, is the centerpiece of their efforts to fabricate a conflict in the circuits on the issue of nonparty shareholder standing. *Marino* stands as an unyielding barrier to *certiorari*, and Petitioners seem to recognize it as such, because they do little more than call it names. A portion of *Marino* which the Seventh Circuit quoted, for example, is dubbed "a gloss of inessential language," and "a single aside." (Petition at 9) Later, the same language becomes "a lone paragraph," (Petition at 12) and then "unnecessary." (Petition at 19)

What Petitioners seek to obscure is the very real force of *Marino*. There, this Court first stated:

> [W]e hold that because petitioners were not parties to the underlying lawsuit, and because they failed to intervene for purposes of appeal, they may not appeal from the consent decree approving that lawsuit's settlement;

484 U.S. at 304. In the next sentence of the opinion, this Court emphasized the lack of controversy over this principle:

> The rule that only parties to a lawsuit, or those that properly become parties, may appeal an adverse judgment, is well settled.

Id. The Court then addressed the view of the court of appeals and politely rejected it:

> The Court of Appeals suggested that there may be exceptions to this general rule, primarily "when the nonparty has an interest that is affected by the trial court's judgment." 806 F.2d at 1152. We think the better practice is for such a nonparty to seek intervention for purposes of appeal; denials of such motions are, of course, appealable.

Id.

It is the last quoted sentence that Petitioners identify as the basis for the Seventh Circuit's ruling here because, when read in isolation, the words may suggest that an appellate court can exercise discretion in permitting a nonparty's appeal. The preceding sentences, however, show that this Court made no such suggestion. After holding without reservation that nonparties may not appeal from approval of a settlement, this Court underscored the point by noting that the rule is well settled. Then, turning to the court of appeals' conflicting view, this Court rejected it by endorsing intervention as the "better practice." This Court did not say intervention was the "better practice" only under the facts presented in *Marino* or in any other particular kind of case. The words were simply a reiteration of what this Court had just held:

> because petitioners were not parties to the underlying lawsuit . . . they may not appeal

> from the consent decree approving the lawsuit's settlement.

484 U.S. at 304.

In view of *Marino's* mandate alone, the prudent course for Petitioners would have been to intervene in the district court before final approval of the settlement. They gambled on whether the Seventh Circuit would follow *Marino* and, not unpredictably, they lost. They should now have no recourse in a writ of *certiorari*.

B. The Seventh Circuit's Ruling Does Not Raise a Conflict Among the Circuits

Petitioners characterize the circuits as "irreconcilably split over whether nonparty shareholders must intervene as parties in order to appeal adverse judgments." (Petition at 11) According to Petitioners, "[t]he Third, Tenth, and (until now) Seventh Circuits have all approved nonparty shareholder appeals." (Petition at 12) These statements are wrong, first, in exaggerating whatever inconsistency exists among the circuits and second, in suggesting that the Seventh Circuit abruptly and independently changed its view on the issue. In fact, only one decision from the Third Circuit, which failed to follow this Court's holding in *Marino* and is in any event distinguishable, differs from the result in the Seventh Circuit. Moreover, the Seventh Circuit very predictably followed *Marino* and even heralded the outcome below by following *Marino* in another case, decided prior to the district court's approval of the settlement here, where the court dismissed appeals of nonparty class members. *See In Re Brand Name Prescription Drugs Antitrust Litigation*, 115 F.3d 456 (7th Cir. 1997).

1. The Purported Split of Authority

The sole case forming the basis for Petitioners' claim of an "irreconcilable split" in the circuits is *Bell Atlantic Corp. v. Bolger*, 2 F.3d 1304 (3d Cir. 1993). Petitioners, however, boldly misrepresent to this Court that another case, *Gottlieb v. Wiles*, 11 F.3d 1004 (10th Cir. 1993), is also in conflict with the Seventh Circuit. (Petition at 2, 8, 12) *Gottlieb* involved settlement of a class action under Rule 23, which, as both the *Gottlieb* court and the Seventh Circuit here noted, is quite different from settlement of a derivative action. 11 F.3d at 1010-11; Petition at 4a-5a. More important, while Petitioners may attempt to rely upon *Gottlieb's dicta* concerning derivative suits, the Tenth Circuit's holding is "that standing is dependent upon a grant of intervention . . . ." 11 F.3d at 1006. *Gottlieb* is thus not only off point but also contrary to the outcome which Petitioners advocate. Petitioners also seem to infer a conflict from *Rosenbaum v. MacAllister*, 64 F.3d 1439 (10th Cir. 1985), but that case involved an appeal from an award of attorneys' fees, not approval of a settlement. No Tenth Circuit case, then, is at odds with the Seventh Circuit here. This leaves only *Bell Atlantic*.

The court in *Bell Atlantic* was faced with nonparty appeals from approval of a derivative suit settlement, but the result it reached was based on Rule 23 class action precedent and analysis. In fact, as the court began that analysis, it noted that "we need not decide whether different rules apply to objector appellate standing in class and derivative suits." 2 F.3d at 1307, n.4. After reviewing the cases in other circuits concerning class action settlements, the court turned to its own decision in *Ace Heating & Plumbing Co. v. Crane Co.*,

453 F.2d 30 (3d Cir. 1971)—also a class action case. *Ace*, which involved settlement of nationwide antitrust litigation, raised issues concerning the effect of class members' failure to opt out of the settlement upon their right to appeal. The *Bell Atlantic* court, after considering the "broad view of objector standing embodied in *Ace*," concluded that the shareholders "had standing to appeal" the order approving settlement. 2 F.3d at 1310.

The *Bell Atlantic* court did raise policy considerations—shareholders' difficulty in monitoring and controlling their attorney, collective action of plaintiffs' attorneys and defendants, and "informational constraints" when the attorneys for both sides present a settlement to the court for approval—but none of these considerations is peculiar to derivative actions. *See* 2 F.3d at 1309-10. The Third Circuit did not address the factors which the Seventh Circuit considered determinative in a strict derivative suit context, *i.e.*, the derivative claim belongs to the corporation not the shareholders, the shareholders are not the injured parties, and as a consequence, their citizenship is ignored when determining diversity, and they are not allowed to opt out. (Petition at 4a-5a)

Bell Atlantic, then, stands not so much as a counterpoint to the Seventh Circuit's rule disallowing nonparty appeals in derivative suits as another opinion treating the issue of such appeals in a broader context including class actions. Moreover, the *Bell Atlantic* court did not take a position directly opposing the Seventh Circuit on the impact of *Marino*. Where the Seventh Circuit found *Marino* controlling, the Third Circuit merely quoted it for the general rule that only parties may appeal an adverse judgment, 2 F.3d at 1307, before moving on to its

own analysis of the issue. *Bell Atlantic* thus never came to grips with *Marino*; the opinion does not reject an argument that *Marino* is controlling, nor does it hold that an exception to the *Marino* rule exists for nonsettling parties in derivative actions. Any court in the future considering those issues thus should have no difficulty in reconciling *Bell Atlantic* with the Seventh Circuit's rule. *Bell Atlantic* is readily viewed as essentially a class action opinion that in any event did not directly address *Marino*, whereas the Seventh Circuit's opinion strictly focused upon a derivative action scenario and firmly held that *Marino* controls.

2. The State of the Law in the Seventh Circuit

Petitioners attempt to bolster a weak *Bell Atlantic* argument and enhance the appearance of a split in the circuits by noting that the Seventh Circuit had formerly approved nonparty appeals, apparently suggesting that a split exists because the Seventh Circuit is in conflict with itself. (Petition at 12) Apart from making no sense in terms of assessing whether a split in the circuits exists, Petitioners' suggestion distorts what the Seventh Circuit actually accomplished in this case. Faced with the issue of nonparty shareholder appeals, the court first found *Marino* controlling and then of necessity overruled a case predating *Marino*, *Tryforos v. Icarian Development Co.*, 518 F.2d 1258 (7th Cir. 1975), which had stated that the right of nonparty shareholders to appeal was "clear." The court also formally overruled *Research Corp. v. Asgrow Seed Co.*, 425 F.2d 1059 (7th Cir. 1970), "and any other case in this circuit . . . that permits nonparties to appeal from a decision of any kind

in a class action." (Petition at 4a) Thus, the Seventh Circuit did not raise a conflict with an earlier opinion; it quite logically ruled so as to avoid one.

The Seventh Circuit's ruling in this case should have come as no surprise inasmuch as it is consistent with the court's opinion last year in *In Re Brand Name Prescription Drugs Antitrust Litigation, supra*. There the panel, following *Marino*, held that a nonparty in a class action could not appeal from an order granting summary judgment to the defendant. The *Brand Name* ruling came six weeks prior to the district court's fairness hearing in this case, which makes Petitioners' failure to intervene all the more daring. In any event, none of Petitioners' discourse on the Seventh Circuit's own decisions on jurisdiction over nonparties can transform those decisions into a conflict among the circuits.

3. Conclusion

The hollowness of Petitioners' split-in-the-circuits argument may be discerned in just one paragraph of the Petition:

> Nor can the split of authority be reconciled. The Third, Tenth, and (until now) Seventh Circuits have all approved nonparty shareholder appeals. *See, e.g., Bell Atlantic Corp. v. Bolger*, 2 F.3d 1304; *Gottlieb v. Wiles*, 11 F.3d 1004; *Rosenbaum v. MacAllister*, 64 F.3d 1439 (10th Cir. 1985); *Tryforos v. Icarian Dev. Co.*, 518 F.2d 1258. The Seventh Circuit now demands formal intervention, in express "disagree[ment]" with these courts. Pet. App. 7a. [footnote]

(Petition at 12) Petitioners appear to set up a conflict involving three circuits and four separate opinions. The

cases, however, are: *Bell Atlantic*, discussed at length above; *Gottlieb*, the class action case which does not follow *Bell Atlantic* and in fact rejects the notion of nonparty appeals; *Rosenbaum*, which is distinguishable on its facts; and, finally, *Tryforos*, the case overruled by the Seventh Circuit because it predated *Marino*. In short, the case for a split of authority boils down to *Bell Atlantic* alone. The last sentence of the quoted paragraph misrepresents what the Seventh Circuit itself said about a conflict, as Petitioners pluck the word "disagree" from a sentence where the court said only that it disagreed with the conclusion in *Bell Atlantic* and transform it into the Seventh Circuit's "disagreement" with the plural, "these courts." The footnote to the paragraph contains only a lengthy citation to what are admittedly Rule 23 class action cases. Such artifice cannot support a grant of *certiorari*.

C. The Seventh Circuit's Decision Requiring Intervention Is Consistent with Rule 23.1 and with Traditional Common Law and Federal Practice

Petitioners warn that their imaginary split in the circuits has "tremendous practical consequences for all nonparty shareholders and the integrity of the shareholder derivative suit process." (Petition at 13) Petitioners argue (1) that requiring intervention is contrary to an overall policy favoring participation by nonparty shareholders in the judicial settlement process (Petition at 14); and (2) that the "Seventh Circuit's shareholder intervention mandate is wrong as a matter of law," being contrary to both Rule 23.1 and common law. (Petition at 17-18) Neither of these arguments is persuasive.

1. Participation By Nonparty Shareholders

Petitioners fill a large segment of their Petition with lengthy citations to authority for the proposition that participation of nonparty shareholders in the judicial settlement process is "a key procedural countermeasure for exposing and preventing . . . corruption." (Petition at 14-15) ADM's Directors do not dispute that general proposition, as far as it goes. The problem with Petitioners' argument, however, is that the general principle does not, under *Marino*, extend to an appeal by nonparty shareholders who have not intervened as parties. The authority Petitioners cite merely endorses the system mandated by Rule 23.1 where nonparty shareholders are given notice and an opportunity to be heard prior to the district court's ruling on a proposed settlement. If a nonparty shareholder seeks involvement beyond that stage, intervention is the obvious next step.

Petitioners complain, however, that intervention imposes a hugely increased financial burden on a shareholder. (Petition at 15-16) To whatever extent such a burden actually exists, Petitioners again miss the point. Intervention is necessary because *Marino* directs that a court of appeals cannot have jurisdiction over a nonparty's appeal from a district court's order approving settlement. Petitioners' argument, then, boils down to the illusory conflict among the circuits in which Petitioners posit that shareholders are faced with a dilemma over intervention. No such dilemma exists; intervention is required.[2]

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[2] Petitioners cite to three circuit court cases which supposedly stand for the "settled law in the Seventh Circuit and elsewhere [which] strongly disfavors intervention after a tentative settlement is reached." (Petition at 16 n.18, *citing Farmland Dairies v. Comm'r of New York State Dep't of Agric. & Markets*, 847 F.2d 1038, 1043-44 (2d Cir. 1988); *Jones v. Caddo Parish Sch. Bd.*, 735 F.2d 923 (5th Cir. 1984); *Ragsdale v. Turnock*, 941 F.2d 501, 504 (7th Cir. 1991). None of these cases, however, involved a derivative suit or class action settlement, and, more important, none contains any general statement that intervention is disfavored after a settlement is reached. Each case simply considers the attempted intervention before it and applies the standards of Rule 24, which require that intervention be timely. In any event, *Marino* makes intervention the only course for nonparty shareholders who wish to preserve their right to appeal. So long as that course is followed in a timely way, courts may permit a nonparty to intervene, and of course denial of intervention is subject to appeal.

(continued...)

2. Rule 23.1 and Common Law

Petitioners argue that the Seventh Circuit's "newly fashioned rule" is inconsistent with the purposes of Rule 23.1 and "in tension with common law practice." (Petition at 17-18) On the first point, Petitioners merely reiterate that the rule does not encourage fair settlement. On the second point, Petitioners cite to a treatise by "English legal scholar Frederic Calvert" published in 1846 and another treatise by Joseph Story published in 1840. As the Seventh Circuit observed concerning similar efforts by Petitioners, they "boil down to a claim that erroneous decisions should be reversed, but arguments of this stripe do not justify omitting the step of intervening as a party." (Petition at 3a) The Seventh Circuit understood that, in a derivative action, "the individual investor is not an injured party and is not entitled to litigate." (Petition at 5a) Rather, suit is brought

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[2] (...continued)

"in the corporation's (not the investor's) right to recover for injury to the corporation." (*Id.*) Analogizing to a *qui tam* action, the court noted that the investors "just get the ball rolling" and that shareholders "have no more the attributes of parties . . . than when managers settle . . . litigation." (*Id.*) Thus, courts focus on the fairness of the derivative settlement to the corporation. Petitioners' personal effort to challenge that fairness on appeal—when no appeal was taken by the defendants, the corporation, or the plaintiffs representing the interests of the overwhelming majority of shareholders who did not object (all of whom were parties to the actions)—is simply misplaced.

Petitioners make one final assault on *Marino*, suggesting that the Seventh Circuit should have placed more weight on nineteenth century commentary than upon this Court's ruling. (Petition at 18) Petitioners first argue that the language of *Marino* relied upon by the Seventh Circuit ("the better practice is to seek intervention") is "unnecessary" to the holding. As explained in section II.A of this brief, however, it is the *holding* of *Marino*, not the "better practice" language, which dooms Petitioners here. It was the *holding* in *Marino* upon which the Seventh Circuit expressly relied. (Petition at 2a) The "better practice" language was simply a reiteration of the holding.

Petitioners attempt to distinguish *Marino* on its facts, arguing that the nonparties there were not members of "the class whose rights are directly affected by any judgment entered in the case . . . ." (Petition at 19) Again, Petitioners have scrambled Rule 23 analysis and a Rule 23.1 case: shareholders in a derivative suit are *not* direct parties in interest. In any event, the holding of

Marino cuts across both kinds of cases. A court of appeals has no jurisdiction over *any* appeal by a nonparty from approval of a settlement.

Petitioners point to *United States ex rel. Louisiana v. Jack*, 244 U.S. 397 (1917), the "lone case" cited in *Marino*, as establishing that "part[ies] *and priv[ies] to the record*" may appeal an adverse decision. (Petition at 19; emphasis by Petitioners) According to Petitioners, "nonparty shareholders are at least 'privy to the record' in derivative suits," although they cite no authority for that proposition, nor offer any definition of the term. (Petition at 20) Petitioners contend that "much settled law would have to be over-turned" if only parties to lawsuits may appeal, and proceed to cite numerous examples where "[n]onparties affected by trial court judgments are treated by the federal courts as 'de facto' parties and permitted to appeal without intervention . . . ." (*Id.*) The trouble with Petitioners' examples is that each involves a court order formally addressed to a nonparty, thus providing appellate jurisdiction.

In one of Petitioners' examples, where a court held a nonparty witness in contempt, the court exercised its contempt jurisdiction over the witness. (Petition at 21 n.22) In another set of examples, Petitioners rely on decisions in which courts that denied an award of attorneys' fees had exercised jurisdiction over the attorneys. (Petition at 21 n.23) And finally, Petitioners point to decisions where a court heard a nonparty who was obligated to the defendant for amounts paid under the court's judgment, after the court had gained jurisdiction by reason of the judgment. (Petition at 21 n.24) None of these examples is affected by the *Marino* rule; each

affected "nonparty" had a separate avenue of appeal to protect his personal interests.

The whole point of *Marino* and the Seventh Circuit here is that an appellate court must have jurisdiction over a person in some individual capacity before that person can participate in appellate proceedings; whether that jurisdiction arises from the court's initiative or action by a potential party is irrelevant. Even Petitioners, as preface to a string citation of cases purporting to support their position, state that "federal courts routinely permit nonparty appeals from judgments that bind the nonparty *by name*." (Petition at 20; emphasis added) Petitioners thus acknowledge that the court involved must take some action relating to a particular individual for appellate jurisdiction to arise.

Petitioners next criticize the Seventh Circuit's reliance on Federal Rule of Appellate Procedure 3(c), which provides that a "notice of appeal must specify the *party or parties* taking the appeal . . . ." (Petition at 2a; emphasis the court's) It was *Marino*, however, not the rule, that formed the basis for the court's ruling. The rule merely reflects the settled principle stated in *Marino*. Petitioners are correct in saying that Rule 3(c) "hardly purports to delineate what matters are inherently eligible or ineligible for appeal" (Petition at 22), but that delineation, contained in *Marino* and elsewhere, draws one bright line: only parties may appeal from approval of a settlement.

Petitioners also seek to use Rule 3(c) affirmatively, first by arguing from provisions concerning class actions, which have no application here and then, incredibly, by redrafting the rule:

> . . . a nonparty shareholder *can* strictly comply with the Rule's language simply by "specify[ing]" that no party is taking the appeal, and "naming each [nonparty] appellant in either the caption or the body of the notice of appeal."

(Petition at 23) Aside from its boldness in adding new terms to the rule, this statement belies Petitioners' statement, made only a page earlier, that "Rule 3(c) hardly purports to delineate what matters are inherently eligible or ineligible for appeal." (Petition at 22) Whether viewing the rule as it is written or as edited by Petitioners, this Court's soundly reasoned opinion in *Marino* takes precedence.

III. THE SEVENTH CIRCUIT'S DECISION TO APPLY ITS RULING RETROACTIVELY IS DICTATED BY PRECEDENT OF THIS COURT, RAISES NO CONFLICT IN THE CIRCUITS, AND CAUSES NO UNFORESEEABLE HARM TO PETITIONERS

Petitioners argue that the Seventh Circuit's "newly formulated" prohibition of nonparty appeals should be applied only prospectively because Petitioners relied on "settled" Seventh Circuit appellate procedures at the time they appealed. (Petition at 23-24) This approach ignores the controlling precedent of this Court and what should have been the obvious import of *Marino* and *In Re Brand Name Prescription Drugs*.

In beginning their argument, Petitioners attempt to color the situation with a quote from Justice O'Connor's dissent in *Harper v. Virginia Dep't of Taxation*, 509 U.S. 86, 113 (1993): "[t]his Court's retroactivity jurisprudence has become somewhat chaotic in recent years." (Petition at 23) *Harper*, however, was a case involving the ret-

roactivity of a Virginia statute taxing federal retirees. There was no jurisdictional issue, and this Court cited no cases dealing with the retroactive application of a decision that an order is not appealable. This Court's jurisprudence on retroactivity in those kind of cases is a model of clarity which even Petitioners do not challenge directly.

The Seventh Circuit followed those clear rules in relying principally on *Firestone Tire & Rubber Co. v. Risjord*, 449 U.S. 368, 379 (1981), where this Court held that a "court lacks discretion to consider the merits of a case over which it is without jurisdiction, and thus, by definition, a jurisdictional ruling may never be made prospective only." (Petition at 7a) In the face of *Firestone*, Petitioners again contrive a momentous split in the circuits, yet once again the "split" shrinks to insignificance upon scrutiny. One case supposedly "in conflict with the decision here" is *Pettyjohn v. Shalala*, 23 F.3d 1572 (10th Cir. 1994), which, according to Petitioners, held "that nothing in *Firestone* requires retroactivity in jurisdictional disputes where appellants would be barred from ever raising their issues before a court of appeals." (Petition at 25) That characterization is pure fiction. First, *Pettyjohn* was not even a case involving a jurisdictional dispute; at issue was the timeliness of an attorney's application for fees under the Equal Access to Justice Act. The decision turned on characterization of a remand from the district court to the administrative agency hearing the plaintiff's application for social security disability benefits. The Tenth Circuit's opinion *does not even mention Firestone*. *Firestone* is cited only in the dissent by a district judge sitting by designation and then only to say that "new rules—especially jurisdictional rules—are to be applied retroactively." 23 F.3d at 1575. That sentiment, of course, was shared by the Seventh Circuit here.

The only other case purported to raise a conflict in the circuits is *George v. Camacho*, 119 F.3d 1393 (9th Cir. 1997), where the court overruled an earlier case holding that plaintiffs in the Northern Mariana Islands are afforded a seven-day extension for filing notices of appeal, and gave only prospective effect to a new rule that notices must be filed within the time allotted by the Federal Rules of Appellate Procedure. The Ninth Circuit distinguished *Firestone* as concerning "a different kind of jurisdictional issue than is present in the case before us." 119 F.3d at 1397. The court believed that *Firestone* was based on the lack of finality of the order appealed from and thus there was "no question in *Firestone* of forfeiting anyone's right to appeal permanently." *Id.* The Ninth Circuit simply refused to hold "that appeals that were timely filed under the law in effect at the time of the filing may retroactively be deemed untimely." 119 F.3d at 1404. Not surprisingly, five of the eleven members of the court sitting *en banc* dissented, adhering to *Firestone's* binding mandate.

George is incorrectly decided, but its peculiarity should not deter other courts from following so coherent a precedent as *Firestone*, particularly in view of its similarly forceful progeny, *Budinich v. Becton Dickinson & Co.*, 486 U.S. 196 (1988) and *Christianson v. Colt Indus. Operating Corp.*, 486 U.S. 800 (1988). In any event, a court faced with a nonparty shareholder seeking to appeal in the context of a derivative action should have no difficulty distinguishing *George* as a case strictly limited

to a change in the time allowed for filing an appeal from a distant territory. There is, after all, not even the appearance of a conflict among the circuits on the Rule 23.1 issue addressed by the Seventh Circuit here.

Petitioners offer up various nightmare scenarios that they say will result from the rule that findings of no jurisdiction apply retroactively: systematic denial of review, litigants relying on settled law only to be barred from appeal when that law is overturned in their own cases, and "a bizarre incentive for litigants to file every conceivable paper and motion . . . solely as an insurance policy against a possible change in law." (Petition at 25-26) What Petitioners would have this Court lose sight of, however, is that a single piece of paper would have provided them with that very insurance policy—a petition to intervene. Amid all of their rhetoric about promoting reliance on settled law, Petitioners never face up to *Marino* and *In Re Brand Name Prescription Drugs*, the settled law that existed when they decided not to become parties to this litigation.

In another attempt to evade *Firestone*, Petitioners challenge the Seventh Circuit's "premise" that "[A] court may not in any case, even in the interest of justice, extend its jurisdiction where none exists." (Petition at 10a, 27) According to Petitioners, a court of appeals has "adjudicatory power," deriving from Article III of the Constitution and 28 U.S.C. § 1291, which extends to any person who has the unusual status of "prudential" standing. (Petition at 27-28) In support of this theory, Petitioners cite this Court's decisions in *Bennett v. Spear*, 520 U.S. 154 (1997), and *Allen v. Wright*, 468 U.S. 737 (1984). *Bennett* held that plaintiffs had standing under the "zone of interests" test to bring a citizen suit under the Endangered Species Act. In *Allen v. Wright*, this Court ruled that parents of African-American school children did not have standing to bring a class action against the Internal Revenue Service for failing to deny tax-exempt status to racially discriminatory private schools. In each case, the issue was one of standing, *i.e.*, whether or not plaintiffs met the "case or controversy" requirement of Article III. Petitioners' reliance on these cases reflects their inability (or unwillingness) to distinguish between standing issues and the more fundamental concept of jurisdiction. The Seventh Circuit here had no such difficulty:

> Standing means injury in fact, and a reduction in the market price of one's stock is injury. Parties are a subset of injured persons. Equating injury with party status is exactly the approach disapproved by *Marino*.

(Petition at 7a) In other words, even if a court found that Petitioners have standing because of alleged injury, that status is of no avail unless the court has "adjudicatory power" over Petitioners by reason of their more particular status as parties in the case. As the Seventh Circuit put it: "If the shareholders had appealed to the House of Lords, that tribunal would have dismissed the appeal out of hand. An appeal by nonparties is no different in effect." (Petition at 10a)

In another shot far wide of the mark, Petitioners assert that the Seventh Circuit's opinion can in no event "be squared with" *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982), where this Court held the Bankruptcy Act of 1978 unconstitutional

because it violated Article III's provision that the judicial power of the United States must be vested in courts whose judges enjoy Article III protections and safeguards. The Court made its decision prospective only to avoid inequitable results. (Petition at 28) *Northern Pipeline*, however, was far different in character from a case like *Firestone*, where this Court considered whether a court of appeals—whose constitutionality was unquestioned—could apply a new jurisdictional rule only prospectively. As this Court stated in declining to apply *Northern Pipeline* retroactively, "It is plain that Congress' broad grant of judicial power to non-Article III bankruptcy judges presents an unprecedented question of interpretation of Article III." 458 U.S. at 64.

It is equally plain from this Court's rulings both before and after *Northern Pipeline* that purely jurisdictional decisions must be applied retroactively. Petitioners particularly challenge one of these decisions, *Budinich v. Becton Dickinson & Co.*, *supra*. (Petition at 29-30) There, this Court followed *Firestone* in holding that a jurisdictional ruling may never be made prospective only:

> Since the Court of Appeals properly held petitioner's notice of appeal from the decision on the merits to be untimely, and since the taking of an appeal within the prescribed time is mandatory and jurisdictional, . . . the Court of Appeals was without jurisdiction to review the decision on the merits.

486 U.S. at 202. Petitioners argue first that *Budinich* reflected an exercise of the court's statutory authority under 28 U.S.C. § 1291 as opposed to its "prudential" authority. (Petition at 29) As explained earlier in this

section of the brief, Petitioners' reliance on "prudential authority" is misplaced because it may come into play only when standing is the issue. Next, Petitioners claim that "because *Budinich* announced no new rule of law, it was not eligible for purely prospective application." (Petition at 29) That statement flies directly in the face of this Court's holding, which stated that a jurisdictional ruling may never be made prospective only, "*[r]egardless of whether today's decision works a change.*" 486 U.S. at 202 (emphasis added). Finally, Petitioners attempt to distinguish the "inequitable results" in *Budinich* from those it claims would "flow from retroactive application" here. (Petition at 30) The readiest answer to that argument lies in *Christianson v. Colt Indus. Operating Corp.*, *supra*, upon which the Seventh Circuit relied but which Petitioners do not seek to distinguish or even address. There this Court again followed *Firestone* and laid to rest whatever doubts may have remained about the place of inequitable results—whatever their character—in determining to apply a jurisdictional ruling retroactively:

> The age-old rule that a court may not in any case, even in the interest of justice, extend its jurisdiction where none exists has always worked injustice in particular cases.

486 U.S. at 818. The Seventh Circuit thus correctly followed a strong line of decisions by this Court which hold that, regardless of any other consideration, jurisdictional rulings by their very nature must be retroactively applied. There is no reason for this Court to grant *certiorari* to alter the decision below.

CONCLUSION

For the foregoing reasons, this Court should deny the Petition for Writ of Certiorari.

Respectfully submitted,

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(3)

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IN THE
Supreme Court of the United States
OCTOBER TERM, 1997

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM, *et al.*,
Petitioners,

v.

PAUL FELZEN, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

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BRIEF IN OPPOSITION OF RESPONDENT ARCHER DANIELS MIDLAND COMPANY

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QUESTIONS PRESENTED

1. Should certiorari be granted to review a decision that joined many other Circuits in following an explicit holding of this Court, rejecting an anomalous decision in another Circuit that several years ago did not do so?

2. Should this Court reconsider its repeated holdings that jurisdictional rulings cannot be made prospective only, in a case presenting no compelling reasons for doing so?

LIST PURSUANT TO RULE 29.6

Respondent Archer Daniels Midland Company is a publicly held corporation. It has no parent companies and its nonwholly owned subsidiaries are Alfred C. Toepfer International, Compagnie Industrielle et Financiere, Consolidated Nutrition, L.C., Gruma S.A. de C.V., and Oelmuhle Hamburg AG.

TABLE OF CONTENTS

	Page
QUESTIONS PRESENTED	i
LIST PURSUANT TO RULE 29.6	ii
TABLE OF AUTHORITIES	iv
STATEMENT	1
A. The District Court Proceedings	1
B. The Court of Appeals' Ruling	4
REASONS FOR DENYING THE WRIT	6
I. THE COURT OF APPEALS, LIKE MANY OTHERS, SIMPLY FOLLOWED THIS COURT'S HOLDING IN *MARINO* v. *ORTIZ*	8
A. Previous Disagreement in the Circuits Has Been Disappearing	8
B. This Court Has Rejected Nearly Identical Petitions in the Past	9
C. There Is No Conflict Requiring This Court's Intervention	11
D. The Holding Is Clearly Correct	14
II. NO SUBSTANTIAL ISSUE REGARDING PROSPECTIVITY IS PRESENTED	18
CONCLUSION	21
ADDENDA	
A. Notice of Appeal	1a
B. Objections to Proposed Settlement (excerpt)	3a
C. Declaration of Ann L. Yerger	7a
D. Declaration of Sarah A. B. Teslik	12a

TABLE OF AUTHORITIES

Cases: Page

Ace Heating & Plumbing Co. v. *Crane Co.*, 453 F.2d 30 (3d Cir. 1971) 11, 12
Bell Atlantic Corp. v. *Bolger*, 2 F.3d 1304 (3d Cir. 1993) 5, 6, 8, 11, 12, 15
Bowling v. *Pfizer, Inc.*, 995 F.2d 1066, 1993 U.S. App. Lexis 14739 (6th Cir. 1993) 18
Bowling v. *Pfizer, Inc.*, 14 F.3d 600 (table), 1993 U.S. App. Lexis 33691 (6th Cir. 1993), *cert. denied sub nom. Ridgeway* v. *Pfizer, Inc.*, 513 U.S. 916 (1994) 10, 18
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Bowling v. *Pfizer, Inc.*, 1995 U.S. App. Lexis 38851 (6th Cir. 1995) 18
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In re Brand Name Prescription Drugs Antitrust Litigation, 115 F.3d 456 (7th Cir. 1997) 4, 5, 20
Budinich v. *Becton Dickinson Co.*, 486 U.S. 196 (1988) 7, 19
Carlough v. *Amchem Products, Inc.*, 5 F.3d 707 (3d Cir. 1993) 12
In re Cement Antitrust Litigation, 688 F.2d 1297 (9th Cir. 1982), *aff'd for absence of quorum sub nom. Arizona* v. *United States District Court*, 459 U.S. 1191 (1983) 10
Christianson v. *Colt Industries Operating Corp.*, 486 U.S. 800 (1988) 19

TABLE OF AUTHORITIES—Continued

Page

Cohen v. *Young*, 127 F.2d 721 (6th Cir. 1942) 10
Croyden Associates v. *Alleco, Inc.*, 969 F.2d 675 (8th Cir. 1992), *cert. denied sub nom. Harry and Jeanette Weinberg Foundation* v. *Croyden Associates*, 507 U.S. 908 (1993) 8, 9, 10
E.I. du Pont de Nemours & Co. v. *Train*, 430 U.S. 112 (1977) 6
Firestone Tire & Ruber Co. v. *Risjord*, 449 U.S. 368 (1981) 5, 7, 19, 20
George v. *Camacho*, 119 F.3d 1393 (9th Cir. 1997) 5, 7, 19
Gottlieb v. *Wiles*, 11 F.3d 1004 (10th Cir. 1993) 8, 13, 15, 17
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Harry and Jeanette Weinberg Foundation, Inc. v. *Croyden Associates*, 507 U.S. 908 (1993) 9
Houston v. *Lack*, 487 U.S. 266 (1988) 20
Kahn v. *Chase Manhattan Bank, N.A.*, 131 F.3d 131 (table), 1997 U.S. App. Lexis 33510 (2d Cir. 1997) 17
Kahn v. *Sullivan*, 594 A.2d 48 (Del. 1991) 20
Karcher v. *May*, 484 U.S. 72 (1987) 14
Keith v. *Volpe*, 118 F.3d 1386 (9th Cir. 1997) 14
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Ex parte Leaf Tobacco Bd. of Trade, 222 U.S. 578 (1911) 14
Loran v. *Furr's/Bishop's, Inc.*, 988 F.2d 554 (5th Cir. 1993) 8
Marine Mammal Conservancy, Inc. v. *Department of Agriculture*, 134 F.3d 409 (D.C. Cir. 1998) 16
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TABLE OF AUTHORITIES—Continued

Page

New York v. *Reebok Int'l, Ltd.*, 96 F.3d 44 (2d Cir. 1996) 11
Ridgeway v. *Pfizer, Inc.*, 513 U.S. 916 (1994) 10
Ridgeway v. *Pfizer, Inc.*, 513 U.S. 1103 (1995) 10
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Rosenbaum v. *MacAllister*, 64 F.3d 1439 (10th Cir. 1995) 13, 15
Shults v. *Champion Int'l Corp.*, 35 F.3d 1056 (6th Cir. 1994) 8
Smith v. *Sperling*, 354 U.S. 91 (1957) 5
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Tryforos v. *Icarian Dev. Co.*, 518 F.2d 1258 (7th Cir. 1975), *cert. denied sub nom. Manta* v. *Tryforos*, 423 U.S. 1091 (1976) 4, 15, 20
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United States v. *City of Oakland*, 958 F.2d 300 (9th Cir. 1992) 16
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In re VMS Limited Partnership Securities Litigation, 976 F.2d 362 (7th Cir. 1992) 13, 20
Walker v. *City of Mesquite*, 858 F.2d 1071 (5th Cir. 1988) 8
Webcor Electronics v. *Whiting*, 101 F.R.D. 461 (D. Del. 1984) 15
Weiser v. *Grace*, No. 95-106285 (Sup. Ct., N.Y. County 1996) 3, 20

Statutes:

28 U.S.C. § 2072 14

Rules:

Federal Rules of Appellate Procedure, Rule 3 ..... 4, 11, 12, 14, 16, 17, 18
Rule 4 16

TABLE OF AUTHORITIES—Continued

Page

Federal Rules of Civil Procedure, Rule 23 ..... 13, 16
Rule 23.1 ..... 17, 18
Rule 24 16
Rules of the Supreme Court of the United States, Rule 10(c) 19

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1997

No. 97-1732

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM, *et al.*,
Petitioners,

v.

PAUL FELZEN, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

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BRIEF IN OPPOSITION OF RESPONDENT ARCHER DANIELS MIDLAND COMPANY

STATEMENT

A. The District Court Proceedings.

In 1995 a number of derivative actions brought by shareholders of Archer Daniels Midland Company (ADM) were consolidated for hearing in the United States District Court for the Central District of Illinois. The complaints sought recovery on behalf of the corporation for alleged wrongdoing by ADM board members claimed to have resulted in antitrust violations and consequent loss to the corporation. Two years of discovery and other pretrial matters followed.

Petitioners, California Public Employees' Retirement System (CalPERS) and the Florida State Board of Administration (FSBA), are large state-employee pension

funds that own stock in ADM as well as in many other publicly traded companies. CalPERS is the largest governmental pension fund in the United States, with assets exceeding $110 billion; FSBA's assets exceed $83 billion. A. 4a.[1] Both are members of the Council of Institutional Investors, an association of large pension funds. A. 4a, 11a. In 1996 the Council was contacted about the suit, and discussed it with the plaintiffs' attorneys. A. 7a-8a. In May 1997 counsel for the plaintiffs, the directors, and ADM negotiated a settlement, calling for payment by the directors of $8,000,000 (including $3,920,000 for attorneys fees and expenses), restructuring of the board, and extensive procedures to increase director independence and safeguard against illegal conduct. All ADM shareholders received written notice, and there was publicity in the financial press as well.

In July 1997 the District Court held a hearing on whether to approve the proposed settlement. Petitioners appeared by counsel and, by written briefs, affidavits and oral argument, objected to the proposed settlement. They argued that the settlement's new "corporate governance" procedures should have included even more of the provisions the Council of Institutional Investors advocates for publicly held corporations, and that the allocation for attorneys' fees was excessive. Petitioners filed affidavits that detailed their efforts through the Council to increase independence of directors in corporations, alter voting procedures, and make other internal corporate changes, policies that the Council presses all major corporations to adopt. A. 11a-12a. They explained that:

> "ADM has been a poster child for the corporate governance movement for years. The settlement of this derivative action offers an unprecedented opportunity to implement changes in ADM's bylaws that will benefit ADM and its shareholders. This opportunity should not be squandered."

[1] Citation to "A." are to the Addenda to this brief.

A. 9a. They attached and submitted an article that explained:

> "Trustees and staff of the California Public Employees' Retirement System are developing guidelines to grade companies in Calpers's portfolio on the independence of their boards. Calpers cannot be ignored: Its $80 billion in equities make it one of the nation's largest shareholders and a force to be reckoned with in the governance arena. . . .
>
> "CEOs who resist pressure for strong governance risk having Calpers or regulatory bureaucrats tell them what kind of board they should have . . . ."

A. 16a, 19a. Acknowledging that ADM already had adopted some of the kinds of changes advocated by the Council, its Executive Director called it "surprising and disappointing" that the settlement agreement did not include more—such as some that ADM's shareholders had voted to reject when petitioners had proposed them. A. 15a, 13a.

Petitioners did not move to intervene in the District Court. One of the counsel for the shareholder plaintiffs observed to the District Court that

> "I would also note that [the Council of] Institutional Investors and specifically CalPERS knows how to come in and make itself known when it wants to. It has done it in a litigation pending in the Supreme Court of New York County *In Re: W. R. Grace* where CalPERS saw fit to bring on an order to show cause to make itself either sole or an additional co-lead counsel. They know how to do it when they want to, judge."

Tr. 7/7/97, p. 9. The attorneys for petitioners did not respond to that point, and never explained to the District Court their failure to intervene.

The District Court approved the settlement and entered judgment accordingly. Petitioners thereupon, still with-

out moving to intervene, filed a notice of appeal to the United States Court of Appeals for the Seventh Circuit. Their notice characterized themselves as "Objectors . . . each of whom is entitled to appeal." A. 2a.

B. The Court of Appeals' Ruling.

Some of the respondents moved to dismiss the appeal on the ground that petitioners, because they had chosen to remain nonparties, had no right to appeal. Respondents cited this Court's decision in *Marino* v. *Ortiz*, 484 U.S. 301, 304 (1988), and a Seventh Circuit opinion that had followed *Marino* and held in a class action that "A nonparty has no right to appeal." *In re Brand Name Prescription Drugs Antitrust Litigation*, 115 F.3d 456, 457 (7th Cir. 1997).

Petitioners responded that they had "believed that it was not necessary to burden the district court with a motion to intervene." Memorandum in Opposition to Plaintiffs' Motion To Dismiss, No. 97-282 U.S.C.A., 7th Cir., at 3 n.2 (Aug. 28, 1997). They said that they had relied on a footnote in a pre-*Marino* Seventh Circuit decision, *Tryforos* v. *Icarian Dev. Co.*, 518 F.2d 1258, 1263 n.22 (7th Cir. 1975) (Stevens, J.), *cert. denied sub nom. Manta* v. *Tryforos*, 423 U.S. 1091 (1976). *Id.* at 2.

The Court of Appeals (Posner, C.J., and Flaum and Easterbrook, JJ.) dismissed petitioners' non-party appeal on authority of *Marino* v. *Ortiz* and Rule 3(c), Fed. R. App. P. In an opinion by Judge Easterbrook, the court noted that this Court in *Marino* had held that "The rule that only parties to a lawsuit, or those that properly become parties, may appeal an adverse judgment, is well settled." Pet. App. 1a, quoting 484 U.S. at 304. That decision, the Court of Appeals held, was of course controlling, and reflected the requirement of Rule 3(c) that "A notice of appeal must specify the *party or parties* taking the appeal . . . ." *Id.* at 2a (emphasis in opinion).

The court noted that in *Brand Name, supra*, it had previously applied *Marino* to an attempt by a non-party to appeal a class action judgment, and that the rule for shareholder derivative suits was no different. Pet. App. 4a. In fact, the court observed, shareholder derivative suits were an *a fortiori* context for applying *Marino*, because unlike ordinary class members, shareholders in a derivative action assert no personal claim, but only the interest of the corporation. Pet. App. 4a-5a, citing *Smith* v. *Sperling*, 354 U.S. 91 (1957). The Court of Appeals noted its disagreement with a 1993 Third Circuit decision which with only passing reference to *Marino* had permitted a non-party in derivative litigation to appeal; that opinion, the Court of Appeals observed, had considered only the issue of standing, without analyzing the distinct issue of party status ruled upon in *Marino*. Pet. App. 6a-7a, discussing *Bell Atlantic Corp.* v. *Bolger*, 2 F.3d 1304 (3d Cir. 1993). "Parties are a subset of injured persons. Equating injury with party status is exactly the approach disapproved by *Marino*." Pet. App. 7a.

Finally, the Court of Appeals held, citing *Firestone Tire & Rubber Co.* v. *Risjord*, 449 U.S. 368, 379 (1981), and similar decisions of this Court, that there was no authority to make the jurisdictional ruling only prospective. Pet. App. 7a. It declined to follow a recent Ninth Circuit decision that had made an overruling involving a local rule applicable to the Northern Mariana Islands prospective "on equitable grounds." Pet. App. 7a, citing *George* v. *Camacho*, 119 F.3d 1393 (9th Cir. 1997) (*en banc*). The Court of Appeals added that even if there could exist some "equitable grounds" exception to the rule that jurisdictional rulings may not be prospective only, its holding in this case was not novel and was clearly required by *Marino* and its own prior holding in *Brand Names* that non-parties in class actions may not appeal. Pet. App. 1a-2a.

REASONS FOR DENYING THE WRIT

The judgment that petitioners ask this Court to review simply adds one more to a series in which the various Circuits, obedient to this Court's holding in *Marino* v. *Ortiz*, 484 U.S. 301 (1988), have held that shareholders or class members who do not make the minimal effort of moving to intervene may not appeal a district court's judgment. Although at one time there was a wide disagreement among the Circuits on this point, that has changed, and after *Marino* little if any disagreement remains. One by one, as the Circuits have had occasion to readdress the issue in light of *Marino*, they have been coming into agreement, and any conflicts that existed in the past have been disappearing. Thus the Seventh Circuit, which in 1975 had held otherwise, here confirmed that in light of *Marino*, any of its previous decisions that allowed non-parties in derivative actions to appeal did not accurately state the law.

The petition really is focused not on that ordinary and expectable holding of the Seventh Circuit, which joined many others, but rather on a decision of a panel in the Third Circuit five years ago that relied on a pre-*Marino* decision, considered standing rather than party status, and scarcely addressed *Marino* at all. *Bell Atlantic Corp.* v. *Bolger*, 2 F.3d 1304 (3d Cir. 1993). To the extent that the Third Circuit did not get the message of *Marino* five years ago, there is no reason to believe that it will not ultimately correct its jurisprudence—just as the present case shows that the Seventh Circuit now has done. Any split in the Circuits that once existed has been shrinking, not growing. If the Third Circuit, which so far has never fully addressed the impact of *Marino*, ultimately does so and nevertheless adheres to an anomalous position, there will be ample opportunity to present such a decision from that Circuit for this Court's review when and if it arises. *Cf. E.I. du Pont de Nemours & Co.* v. *Train*, 430 U.S. 112, 135 n.26 (1977) (noting "the wisdom of allowing difficult issues to mature through full consideration by the courts of appeals").

As for the second question the petition seeks to raise, once again, this Court has already firmly settled it. Jurisdictional rulings cannot be made prospective only. *Budinich* v. *Becton Dickinson & Co.*, 486 U.S. 196, 203 (1988); *Firestone Tire & Rubber Co.* v. *Risjord*, 449 U.S. 368, 379 (1981). Nor, even if they could, would there be reason to do so here. This is not a case, like the unusual Ninth Circuit decision petitioners cite, of an abrupt overruling of a court's own precedent on a local rule at the expense of a bewildered litigant. See *George* v. *Camacho*, 119 F.3d 1393 (9th Cir. 1997) (*en banc*). On the contrary, this Court itself has observed that the rule that non-parties may not appeal "is well settled." *Marino*, 484 U.S. at 304. Petitioners have frequently intervened in derivative actions. See p. 20, *infra*. Sophisticated litigants like petitioners, who made a calculated tactical judgment in this case to avoid the obligations of party status, would be in a poor posture to claim ignorance.

As to both the questions petitioners say are presented, they have brushed aside the fact that these points have already been settled both by the weight of circuit authority and by decisions of this Court. Instead, they have struggled to locate in some other Circuit some anomalous case—one that is contrary to this Court's decisions, is not followed in other Circuits, and is significantly factually different besides—and invoke that odd decision as an excuse for seeking certiorari to review the Seventh Circuit's ordinary and well reasoned opinion, which like many others *does* follow this Court's holdings, and actually has *diminished* any previous intercircuit disagreement. There is no need for this Court to revisit these settled issues, and very likely there never will be. Nothing in this case presents an occasion or need for certiorari.

I. THE COURT OF APPEALS, LIKE MANY OTHERS, SIMPLY FOLLOWED THIS COURT'S HOLDING IN *MARINO* v. *ORTIZ*.

A. Previous Disagreement in the Circuits Has Been Disappearing.

Petitioners three times quote the Court of Appeals' observation that "[c]ourts have disagreed for several decades" about whether non-party class members and shareholders may appeal. Pet. Cert. at 2, 11, Reply at 1, quoting Pet. App. 2a. Petitioners also argue that the shareholder respondents "do not offer any means of reconciling this split of authority." Reply at 1.

On the contrary. The Court of Appeals after its language that petitioners quote went on to explain that the decades-old issue was settled when this Court decided *Marino*. Pet. App. 2a-4a. And any remnant of the previous split has been "reconciling" itself. Since *Marino* one Circuit after another in both class actions and derivative suits has been falling into line—just as the Seventh Circuit, which before *Marino* had taken the opposite position, did here. The Seventh here joined five other Circuits. See *Loran* v. *Furr's/Bishop's, Inc.*, 988 F.2d 554 (5th Cir. 1993); *Walker* v. *City of Mesquite*, 858 F.2d 1071, 1075 (5th Cir. 1988); *Shults* v. *Champion Int'l Corp.*, 35 F.3d 1056, 1060-61 (6th Cir. 1994); *Croyden Associates* v. *Alleco, Inc.*, 969 F.2d 675, 680 (8th Cir. 1992), *cert. denied sub nom. Harry and Jeanette Weinberg Foundation* v. *Croyden Associates*, 507 U.S. 908 (1993); *Gottlieb* v. *Wiles*, 11 F.3d 1004, 1009 (10th Cir. 1993); *Guthrie* v. *Evans*, 815 F.2d 626, 627 (11th Cir. 1987) (*pre*-Marino).

All that today remains of the anti-*Marino* position is a 1993 Third Circuit opinion, *Bell Atlantic, supra*, whose authority is undercut by its complete failure to address the issue of party status as distinct from standing, and its failure to reconcile its view with *Marino*. Like the Cheshire Cat, the anti-*Marino* jurisprudence has been steadily fading from view. Only a feeble smile—a Third Circuit decision of five years ago that did not analyze the issue—remains.

What petitioners present is an issue of past nonconformity by the Third Circuit with a decision of this Court, not a split among two groups of Circuits on some major issue this Court has yet to address. If five years ago the Third Circuit failed to analyze *Marino* and follow it, that raises no need to review this case, in which the Seventh Circuit like many others did so. If rejection of *Marino* turns out really to be the current Third Circuit view, there will be future opportunities to review such a Third Circuit decision when and if the need arises.

B. This Court Has Rejected Nearly Identical Petitions in the Past.

This Court on at least four occasions has denied petitions for certiorari just like the one here. And its wisdom in doing so has been vindicated, as division in the Circuits has steadily shrunk.

When the Eighth Circuit, citing *Marino* v. *Ortiz*, held that non-party class members may not appeal, that court like the Seventh Circuit here wrote a thoughtful and strong opinion, which even commented, discussing cases from the Third and Seventh Circuits, that "[t]he circuits are divided on this issue." *Croyden Associates* v. *Alleco Inc.*, 969 F.2d 675, 678 (8th Cir. 1992). The non-parties then urged this Court that "The Eighth Circuit's Decision Is In Conflict With Decisions of Other Courts of Appeal," referring particularly to decisions in the Sixth, Seventh and Third Circuits. Petition for Writ of Certiorari, *Harry and Jeanette Weinberg Foundation, Inc.* v. *Croyden Associates*, No. 92-613, OT 1992, at 8 (1992). This Court denied certiorari. *Harry and Jeanette Weinberg Foundation, Inc.* v. *Croyden Associates*, 507 U.S. 908 (1993).

Next the Sixth Circuit, in spite of a prior holding,[2] announced that non-party class members who had not moved to intervene could not appeal. *Bowling* v. *Pfizer, Inc.*, 14 F.3d 600 (table), 1993 U.S. App. Lexis 33691 (6th Cir. 1993). Once again there was a petition for certiorari, arguing that "There Is A Deep Split In The Circuits," referring this time to decisions in the Seventh and Third. Petition for Writ of Certiorari, *Ridgeway* v. *Pfizer, Inc.*, No. 93-1912, OT 1993, at 12 (1994).[3] Once again, this Court denied certiorari. *Ridgeway* v. *Pfizer, Inc.*, 513 U.S. 916 (1994).

The following Term, this Court was petitioned again to review the issue of non-party appeals, those petitioners claiming that they had lacked a "crystal ball" and so could not have predicted that the Sixth Circuit would follow this Court's decision in *Marino* instead of its own earlier cases. Petitioners' Reply Brief in Opposition, *Ridgeway* v. *Pfizer, Inc.*, No. 94-843, OT 1994, at 8 (1994). This Court once again denied certiorari. *Ridgeway* v. *Pfizer, Inc.*, 513 U.S. 1103 (1995). The same petitioners later raised the issue again, and this Court denied certiorari again. *Ridgeway* v. *Pfizer, Inc.*, 118 S. Ct. 263 (1997) (No. 97-47).

Only one thing has changed in the interval: the pre-*Marino* split in the Circuits has continued to get smaller. For now the Seventh Circuit, previously aligned with the Third, has acknowledged *Marino* and unequivocally joined the other Circuits. This leaves the Third Circuit, to the extent it can be thought to have a post-*Marino* position, all alone.

Petitioners argue that "[t]he panel below virtually invited certiorari." Pet. Cert. 11. But no more than had the Eighth Circuit in *Croyden Associates* when it noted the

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2 See *Cohen* v. *Young*, 127 F.2d 721, 724 (6th Cir. 1942).

3 The petition also cited a pre-*Marino* decision of the Ninth Circuit, *In re Cement Antitrust Litigation*, 688 F.2d 1297 (9th Cir. 1982), *aff'd for absence of quorum sub nom. Arizona* v. *United States District Court*, 459 U.S. 1191 (1983).

much wider disagreement in 1993. The Seventh Circuit in its thorough and candid opinion simply acknowledged that some inconsistent authority remained on the books, and pointed out that the Third Circuit had never analyzed the issue of party status as distinct from standing, and was not to be followed because of this Court's holding in *Marino*. Pet. App. 6a-7a. Moreover, this Court has no practice of automatically granting certiorari whenever one court notes disagreement with another, or even when (not the case here) a court of appeals requests it.[4]

C. There Is No Conflict Requiring This Court's Intervention.

The Fifth, Sixth, Eighth, Tenth and Eleventh Circuits all agree with the Seventh. See p. 8, *supra*. The Second by implication does also. See *New York* v. *Reebok Int'l, Ltd.*, 96 F.3d 44, 48 (2d Cir. 1996) (holding that under *Marino* non-parties could not appeal settlement of *parens patriae* litigation). There are no post-*Marino* cases that disagree except, as of 1993, in the Third. In 1971 that Circuit, without ever adverting to the issue of intervention, held that class members who had not opted out had "standing to appeal" a settlement. *Ace Heating & Plumbing Co.* v. *Crane Co.*, 453 F.2d 30, 33 (3d Cir. 1971). In 1993, under the heading "Standing," the Third Circuit held that its holding in *Ace Heating* was dispositive in a shareholder derivative action, and that "[t]hough *Ace* did not discuss whether objecting class members should be required to intervene as a condition for appellate standing, rejection of such a requirement was essential to its reasoning and result." *Bell Atlantic Corp.* v. *Bolger*, 2 F.3d 1304, 1309 (3d Cir. 1993). The opinion mentioned in passing *Marino* and Rule 3(c), Fed.

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4 *Cf. Mayes* v. *Pickett*, 537 F.2d 1080, 1083-84 (9th Cir. 1976) ("Perhaps this case presents a record which will attract the attention of the Supreme Court. The conflict between the circuits should be settled."), *cert. denied sub nom. United States* v. *Mayes*, 431 U.S. 924 (1977) (denying petition of United States).

R. App. P., 2 F.3d at 1307, but adhered to its pre-*Marino* case. The opinion gave weight to what it perceived as "risks flowing from shareholders' difficulty in monitoring derivative litigation," concluding that "[g]iven the agency, collective action, and information problems inherent in settlements of derivative litigation, and the broad view of objector standing embodied in *Ace*, we conclude Lazar had standing to appeal the district court order approving the settlement." 2 F.3d at 1310.

At most the holding of the Third Circuit panel five years ago in *Bell Atlantic* represents an anomalous ruling that failed to distinguish standing from the requirements of Rule 3(c) and *Marino*, and has not been followed by other courts of appeals—which is not surprising, given this Court's clear holding in *Marino*. There is no reason for this Court to revisit settled law now—particularly when the practical effect is so small, because under *Marino* all that an objector need do to ensure an appeal right is move to intervene. If the Third Circuit finally analyzes the issue and then persists in ignoring this Court's ruling, there will be time enough, if it then seems appropriate, to review a Third Circuit case failing to follow *Marino*.[5]

Petitioners also, although more haltingly, claim a conflict with the Tenth Circuit, but the cases show just the opposite. The Tenth Circuit in a class action case very clearly held that

> "For the above reasons, we agree with the Eleventh Circuit that formal intervention is a prerequisite to an unnamed class member's standing to appeal . . . . We note that the Eighth and Fifth Circuits have recently come to the same conclusion."

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[5] The reasoning of *Bell Atlantic* was already undercut in the Third Circuit a month later in *Carlough* v. *Amchem Products, Inc.*, 5 F.3d 707 (3d Cir. 1993), which in holding that a class member who *did* move to intervene would be allowed at some point to appeal, specifically distinguished cases in which class members or shareholders had not moved to intervene. See 5 F.3d at 713-14.

Gottlieb v. *Wiles*, 11 F.3d 1004, 1009 (10th Cir. 1993). In fact, its opinion added presciently that "we believe that the tone of *VMS* indicates that the Seventh Circuit will ultimately adopt the rule we set forth today." *Id.* at 1011, referring to *In re VMS Limited Partnership Securities Litigation*, 976 F.2d 362 (7th Cir. 1992).

A subsequent Tenth Circuit opinion reiterated and confirmed that holding, explaining that "This court has recently joined the circuits that require intervention by a class member in a Rule 23(b)(3) case in order to have standing to appeal the district court's approval of the settlement." *Rosenbaum* v. *MacAllister*, 64 F.3d 1439, 1442 (10th Cir. 1995). Although in dictum suggesting that its *Gottlieb* opinion did not necessarily control in a derivative suit, the court nevertheless strongly endorsed *Gottlieb*'s reasoning in terms that apply to both:

> "To allow a nonintervening class member to appeal approval of a settlement would permit one dissent—and there is likely always to be one—to postpone realization of any of the benefits that might otherwise come to the class members and to prevent the defendant from settling its liability."

64 F.3d at 1442. The case went on to conclude that the rule need not apply when, unlike here, the non-party did not challenge the settlement, and there was only a dispute over attorneys' fees. Whether or not that distinction, which no other case has followed, is correct, it would not apply here, for petitioners as non-parties attempted to appeal the entire setlement. On that issue, the position of the Tenth Circuit is firmly with that of the Seventh and others.

Petitioners attempt to distinguish some of the post-*Marino* cases on the ground that the attempts by non-parties to appeal arose in class actions, not derivative suits. Pet. 12 n.10. But as the Court of Appeals pointed out, derivative suits are logically an even more obvious case for application of *Marino*. Pet. App. 4a. Indeed, if this Court ever thought there was some need to reexamine *Marino*, the better vehicle for doing so would be an ordi-

nary class action, in which, unlike derivative suits, the class members at least have claims to assert in their own right. Certainly the present decision, simply joining others in following *Marino*, does not create any serious and live disagreement in the lower courts that requires this Court's intervention at this time.

D. The Holding Is Clearly Correct.

The Court of Appeals' reasoning is exceptionally clearly stated and need not be reiterated here. The logic of its holding is confirmed by the fact that since *Marino* (and in some instances before), at least five other Circuits have held the same thing.

According to petitioners, Rule 3(c) is "far too thin a reed." Pet. Cert. 22. But it is a duly adopted rule that has the force of law, and "a jurisdictional prerequisite." *Torres* v. *Oakland Scavenger Co.*, 487 U.S. 312, 318 (1988); 28 U.S.C. § 2072. This Court found it authoritative in *Marino*, 484 U.S. at 304. Petitioners also argue that Rule 3(c) should have been treated as merely restating prior law. But in *Marino* this Court held that it did just that, citing as an example of prior law *United States ex rel. Louisiana* v. *Jack*, 244 U.S. 397, 402 (1917); see also, *e.g.*, *Karcher* v. *May*, 484 U.S. 72, 77 (1987); *Ex parte Leaf Tobacco Bd. of Trade*, 222 U.S. 578, 581 (1911) ("[o]ne who is not a party to a record and judgment is not entiled to appeal therefrom").[6]

The petition includes citations to commentators. Some of those are policy discussions, more properly addressed to legislation or rulemaking than to adjudication. And those that petitioners cite as summarizing the law turn out to provide little support for petitioners' position:

—For example, petitioners twice quote a line from one treatise that "objector to the settlement may appeal the

[6] Intervention is not necessary for appeal when a district court itself has effectively conferred party status by directing an order against the appellant personally. *E.g.*, *Keith* v. *Volpe*, 118 F.3d 1386, 1391 n.7 (9th Cir. 1997); see also examples at Pet. Cert. 20 n.21.

court's approval of the compromise." Pet. Cert. 8 n.8, Reply at 4 n.5, quoting 7C C. WRIGHT, A. MILLER & M. KANE, FEDERAL PRACTICE & PROCEDURE § 1839 at 182 (2d ed. 1986). Those words do appear, without discussion or analysis, in the treatise; but the only authority the treatise cites for them is a passing dictum in a footnote in a pre-*Marino* district court case from the Third Circuit.[7] Elsewhere the same commentators acknowledge that while they believe in some circumstances class members ought to be allowed to appeal,

> "it has been ruled that an individual class member who has not been recognized as a class representative and who has not intervened lacks standing to appeal a judgment on the merits. Similar rules may apply to corporate shareholders affected by the judgment in a derivative action."

15A *id.* § 3902.1 at 105-06 (footnotes omitted).[8]

—Moore's treatise, which petitioners also cite, refers to a "split in authority"—as to which it cites pre-*Marino* cases, with no post-*Marino* cases supporting petitioners' position except in the Third Circuit.[9] See 5 J. MOORE, MOORE'S FEDERAL PRACTICE § 23.1.10[3] (3d ed. 1998).[10]

[7] *Webcor Electronics* v. *Whiting*, 101 F.R.D. 461, 465 n.11 (D. Del. 1984). The supplement updating the same page of the treatise adds reference to the Third Circuit's *Bell Atlantic* case—stating in boldface that the opinion cited the treatise—but fails to mention any of the many contrary decisions, or even *Marino*. 7C C. WRIGHT *et al.*, 1998 Supp. at 13 n.22.

[8] Petitioners' opening quote to Wright & Miller is out of context and does not deal with non-party appeals at all. *Compare* 7C WRIGHT *et al.* § 1839 at 175 *with* Pet. Cert. 2 n.1. Their quote from a law encyclopedia, 10 FEDERAL PROCEDURE, LAWYERS EDITION 260 (1994), see Pet. Cert. 8 n.8, relies entirely on the Seventh Circuit's overruled *Tryforos* decision.

[9] It notes that the Tenth Circuit in *Gottlieb* held that non-parties may not appeal a settlement, citing also the *Rosenbaum* decision regarding a limited attorneys' fees challenge, discussed *supra* p. 13.

[10] Petitioners five times invoke a comment by a law student who criticized this Court's holding in *Marino*. Pet. Cert. 13, 18 (twice),

Petitioners' speculation that intervention motions would likely be denied, Reply at 6, is both unsupported and beside the point. Rule 24, Fed. R. Civ. P., allows intervention even after judgment, see *United Airlines, Inc.* v. *McDonald*, 432 U.S. 385 (1977), and the reports are full of cases in which intervention in shareholder suits and derivative actions has been unhesitatingly granted. Moreover, as this Court pointed out in *Marino*, once a shareholder moves to intervene, the denial of such a motion itself is "of course" appealable. 484 U.S. at 304.[11]

Petitioners' policy arguments—that intervention somehow imposes a terrible (albeit vaguely described) burden on dissident shareholders—have an especially hollow ring in the circumstances of this case. Moving to intervene is scarcely a forbidding burden, particularly for gigantic organizations like petitioners, who have their own well-publicized agenda for altering the governance of U.S. corporations by means of litigation. See A. 6a, 8a-9a.

The petition also surely exaggergates in asserting that "[a] key procedural safeguard against collusion and abuse is also at stake," Pet. Cert. 14, simply because one more

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Reply 6, 8; Duffy, *The Appealability of Class Action Settlements by Unnamed Parties*, 60 U. CHI. L. REV. 933, 946 (1993). By contrast, the Reporter of the Rules Advisory Committee emphasized that participation by a class member was not intended by the drafters of the Rules to amount to party status. "If 'appearance' [in Rule 23] is read as enabling the class member to be admitted automatically into the action as a party, it would stand in odd contrast to intervention in the action under rule 24 . . . ." Kaplan, *Continuing Work of the Civil Committee: 1966 Amendments of the Federal Rules of Civil Procedure (I)*, 81 HARV. L. REV. 356, 392 n.137 (1967).

11 "Federal appellate courts . . . routinely hear appeals from denials of motions to intervene as of right, even though 'Federal Rules of Appellate Procedure 3 and 4 clearly contemplate that only parties may file a notice of appeal.'" *Marine Mammal Conservancy, Inc.* v. *Department of Agriculture*, 134 F.3d 409, 412-13 (D.C. Cir. 1998), quoting in part *United States* v. *City of Oakland*, 958 F.2d 300, 301 (9th Cir. 1992).

Circuit has held that shareholders must intervene before appealing. Much of the petition is devoted to arguing the benefits of shareholder monitoring of derivative-suit settlements. But that is not at issue. Shareholder procedural rights have been provided and delineated in Rule 23.1, Fed. R. Civ. P. No one is arguing against proper shareholder participation, and neither *Marino* nor the Seventh Circuit's decision nor the many similar decisions in other Circuits significantly affects shareholder rights at all. Objectors who wish to appeal need only move to intervene. Petitioners have never presented any good reason not to have done so. *Cf. U.S. Philips Corp.* v. *Windmere Corp.*, 971 F.2d 728, 730 (Fed. Cir. 1992) (non-party's "asserted interest" questionable when he "refrained from intervention at the trial"), *cert. dismissed sub nom. Izumi Seimitsu Kogyo Kabushiki Kaisha* v. *U.S. Philips Corp.*, 510 U.S. 27 (1993); *Kahn* v. *Chase Manhattan Bank, N.A.*, 131 F.3d 131 (table), 1997 U.S. App. Lexis 33510 at *5 (2d Cir. 1997) ("proposed plaintiffs' failure to move to intervene here, moreover, belies their assertions of a strong interest in this litigation").

Petitioners misunderstand the issue as "a policy decision" involving "purely discretionary, self-imposed restrictions on jurisdiction," "purely prudential." Pet. Cert. 27, 3, 28. As if Rule 3(c) and *Marino* did not exist, they attempt to assemble policy arguments for allowing non-party appeals. There are certainly powerful considerations on the other side as well, considerations that judges recognize better than anyone. As the Tenth Circuit observed with respect to class actions,

> "If individual appeals without formal intervention were to be permitted, the class action would break down under the burden of unpredictable and unlimited individual actions."

Gottlieb v. *Wiles*, 11 F.3d 1004, 1009 (10th Cir. 1993); see also, *e.g.*, *Guthrie* v. *Evans*, *supra*, 815 F.2d at 628 ("class actions could become unmanageable"). Also, there is an "interest in encouraging settlements, particularly in

class actions, which are often complex, drawn out proceedings demanding a large share of finite judicial resources." *Mayfield* v. *Barr*, 985 F.2d 1090, 1092 (D.C. Cir. 1993).[12] In any event, the short answer is that the Federal Rules, as this Court recognized in *Marino*, simply do not enact what petitioners want. See Fed. R. Civ. P. 23.1; Fed. R. App. P. 3(c). Petitioners' less-than-compelling policy arguments should be directed to the policy makers: the Congress, or the drafting committees who recommend Rule changes to this Court.

II. NO SUBSTANTIAL ISSUE REGARDING PROSPECTIVITY IS PRESENTED.

The second question presented in the petition is insubstantial for several reasons.

1. Once again petitioners are challenging something this Court already has firmly and recently decided. In explaining that its jurisdictional ruling could not, as petitioners requested, be made prospective only, the Court of Appeals pointed out that it was simply following unequivocal holdings of this Court. See Pet. App. 8a-10a, citing *Landgraf* v. *USI Film Products*, 511 U.S. 244, 274

[12] The burden on appellate courts is heavy enough without adding appeals of settlements by non-parties. For one example, the Sixth Circuit earlier this year commented in a class action opinion that "[t]he remarkable aspect of this outpouring of judicial resources is that much of it occurred after the case settled." *Bowling* v. *Pfizer, Inc.*, 132 F.3d 1147, 1148 (6th Cir. 1998). Previous appeals in the same case that had required the Sixth Circuit to file opinions or enter orders (also leading to three petitions for certiorari) include: *Bowling* v. *Pfizer, Inc.*, 1997 U.S. App. Lexis 3782 (6th Cir. 1997); *Bowling* v. *Pfizer, Inc.*, 103 F.3d 128 (table), 1996 U.S. App. Lexis 33200 (6th Cir. 1996), *cert. denied sub nom. Ridgeway* v. *Pfizer Inc.*, 118 S. Ct. 263 (1997); *Bowling* v. *Pfizer, Inc.*, 102 F.3d 777 (6th Cir. 1996); *Bowling* v. *Pfizer, Inc.*, 1995 U.S. App. Lexis 38851 (6th Cir. 1995); *Bowling* v. *Pfizer, Inc.*, 14 F.3d 600 (table), 1993 U.S. App. Lexis 34016 (6th Cir. 1993), *cert. denied sub nom. Ridgeway* v. *Pfizer, Inc.*, 513 U.S. 1103 (1995); *Bowling* v. *Pfizer, Inc.*, 14 F.3d 600 (table), 1993 U.S. App. Lexis 33691 (6th Cir. 1993), *cert. denied sub nom. Ridgeway* v. *Pfizer, Inc.*, 513 U.S. 916 (1994); *Bowling* v. *Pfizer, Inc.*, 995 F.2d 1066 (table), 1993 U.S. App. Lexis 14739 (6th Cir. 1993).

(1994); *Harper* v. *Virginia Dep't of Taxation*, 509 U.S. 86, 97 (1993); *Christianson* v. *Colt Industries Operating Corp.*, 486 U.S. 800, 818 (1988); *Budinich* v. *Becton Dickinson & Co.*, 486 U.S. 196, 203 (1988); and *Firestone Tire & Rubber Co.* v. *Risjord*, 449 U.S. 368, 379 (1981). "[B]y definition, a jurisdictional ruling may never be made prospective only." *Firestone*, 449 U.S. at 379.

2. Petitioners rely on a peculiar Ninth Circuit decision which they say is in conflict because the Ninth Circuit applied a jurisdictional ruling prospectively. *George* v. *Camacho*, 119 F.3d 1393 (9th Cir. 1997) (*en banc*). That 6-5 decision, in an opinion by Judge Reinhardt, after describing a highly unusual fact situation, either distinguished or declined to follow this Court's decisions in *Firestone* and *Budinich*, and held that a change in the court's prior holding as to time for certain appeals would be prospective only. There are enormous factual and procedural differences between this case and that one, which involved application of a changed interpretation of an arguably misleading local rule to an unsophisticated litigant in the Northern Mariana Islands.

At best, the opinion in *George* depended upon its own extremely unusual facts. At worst, it appears to be a decision never followed elsewhere and unlikely to be, because "the majority fails to follow clearly applicable Supreme Court precedent." 119 F.3d at 1404 (T. Nelson, J., and four others dissenting). What petitioners call a "considered decision[]," Pet. Cert. 8, another dissent dismissed as "twaddle," "supported by neither law nor justice" and "rest[ing] entirely on air, and not cold air, either." 119 F.3d at 1410-11 (Kozinski, J., joined by O'Scannlain, J., dissenting). The Seventh Circuit cited it only to acknowledge its existence and note its exceptional nature. Pet. App. 7a. Conceivably, if certiorari had been sought in that Ninth Circuit case, there might have been reason, in spite of its unique factual situation, for this Court to

have reviewed it—not as a Circuit conflict, but rather under this Court's Rule 10(c) as a decision "that conflicts with relevant decisions of this Court." But surely such an anomalous opinion, rendered over considerable protest in another Circuit, is no reason whatsoever to review the Seventh Circuit's rather commonplace *adherence*, in wholly different facts, to *Firestone* and the other decisions of this Court.

3. Even if—contrary to this Court's decisions—it were possible based on some case-specific leniency to make a jurisdictional ruling apply only in the future, no reason to do so existed here. Petitioners could not remotely be regarded as unsophisticated in the ways and rules of litigation. *Cf. Houston* v. *Lack*, 487 U.S. 266, 270 (1988) ("The situation of prisoners seeking to appeal without the aid of counsel in unique"). It was actually pointed out to petitioners in the District Court that they had failed to intervene, even though in other derivative actions they had done so. See p. 3, *supra*, referring to *Weiser* v. *Grace* No. 95-106285 (Sup. Ct., N.Y. County) (order Sept. 3, 1996 granting intervention by CalPERS in derivative action); see also, *e.g.*, *Kahn* v. *Sulivan*, 594 A.2d 48, 50 (Del. 1991) (intervention by CalPERS in derivative action).

Petitioners simply deliberately chose not to intervene, and when their appeal was challenged, argued that they had believed the Seventh Circuit's rule was different, based on a footnote in its 1975 *Tryforos* opinion. But as the Court of Appeals made clear, after *Marino* and the Seventh Circuit holdings in *Brand Name* and *VMS*, as well as the many cases in accord in other Circuits, no basis existed for such reliance. In words petitioners apply to others, they "ignored multiple warning signals." Pet. Cert. 30. Petitioners' assertion that in not intervening they relied on "settled law," Pet. Cert. 3, is belied by the very words of this Court: "The rule that only parties to a lawsuit, or those that properly become parties, may appeal an adverse judgment, is well settled." *Marino*, 484 U.S. at 304.

Moreover, petitioners acknowledge that tactical considerations apply to what they did. In their words, as parties

> "they would face all the duties associated with becoming a party, including duties to comply with automatic disclosure requirements, appear for depositions, answer interrogatories, and produce documents."

Reply at 7. Petitioners preferred instead to take a chance. They have no attractive claim for relief from the results of a tactical gamble. This Court's prohibition of prospective-only jurisdictional rulings, now followed by the lower courts dozens if not hundreds of times, need not be revisited, particularly in a case where sophisticated litigants could not have demonstrated any compelling reasons for a special dispensation.

CONCLUSION

For the reasons stated, certiorari should be denied.

Respectfully submitted,

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• Counsel of Record

July 22, 1998

ADDENDA

ADDENDUM A

[Filed Jul. 15, 1997]

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

Case No. 95-2279

Honorable Harold A. Baker
Judge Presiding

PAUL FELZEN, TRUSTEE OF LOUISE LASKIN TRUST—1991 and SANDRA ESNER,
Plaintiffs,

v.

DWAYNE O. ANDREAS, *et al.*,
Defendants,

and

ARCHER DANIELS MIDLAND COMPANY,
a Delaware Corporation,
Nominal Defendant.

IN THE COURT OF CHANCERY
OF THE STATE OF DELAWARE
IN AND FOR NEW CASTLE COUNTY

Consolidated C.A. No. 14403

IN RE: ARCHER DANIELS MIDLAND COMPANY

NOTICE OF APPEAL BY CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM AND FLORIDA STATE BOARD OF ADMINISTRATION

Notice is hereby given that Objectors California Public Employees' Retirement System ("CalPERS") and Florida State Board of Administration ("SBA"), each of whom is entitled to appeal from the Final Judgment and Order of Dismissal (July 7, 1997), and Order Awarding Attorneys' Fees and Reimbursement of Expenses (July 7, 1997), hereby appeal from such Judgment and Order to the United States Court of Appeals for the Seventh Circuit.

A joint appeal is practicable because, as is described in CalPERS and SBA's joint Objections to the Settlement (July 3, 1997), CalPERS and SBA's interests are aligned.

Respectfully submitted,

/s/ Mark C. Hansen
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D.C. Bar No. 425930
STEVEN F. BENZ
D.C. Bar No. 428026
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Attorneys for
California Public Employees' Retirement Systems, Inc. and the Florida State Board of Administration

Date: July 14, 1997

ADDENDUM B

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

Case No. 95-2279

Honorable Harold A. Baker
Judge Presiding

PAUL FELZEN, TRUSTEE OF LOUISE LASKIN TRUST—1991 and SANDRA ESNER,
Plaintiffs,

v.

DWAYNE O. ANDREAS, *et al.*,
Defendants,

and

ARCHER DANIELS MIDLAND COMPANY,
a Delaware Corporation,
Nominal Defendant.

IN THE COURT OF CHANCERY
OF THE STATE OF DELAWARE
IN AND FOR NEW CASTLE COUNTY

Consolidated C.A. No. 14403

IN RE: ARCHER DANIELS MIDLAND COMPANY

OBJECTIONS OF CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM AND FLORIDA STATE BOARD OF ADMINISTRATION TO PROPOSED SETTLEMENT OF DERIVATIVE ACTIONS

* * * *

Interests of the Objectors

Objector California Public Employees' Retirement System ("CalPERS") is the nation's largest governmental ("public") pension fund: it manages assets with a current market value of more than $110 billion on behalf of over one million U.S. citizens who are its employees and beneficiaries. CalPERS currently owns more than 2.8 million shares of ADM stock, and on information and belief is one of the largest single holders of ADM shares.

Objector Florida State Board of Administration ("SBA") is also a large public pension fund, with assets having a market value of over $83.3 billion for the Florida Retirement System Trust Fund, the Local Government Surplus Funds Trust Fund, and other various trust funds on behalf of 586,796 employees and 149,571 current beneficiaries. SBA currently owns 1,765,977 shares of ADM stock.

Objectors CalPERS and SBA are, on information and belief, the largest ADM shareholders that have taken any public position on the proposed Settlement.

Lawyers for the nominal plaintiffs contacted the Council of Institutional Investors ("Council")—a prominent organization of large institutional shareholders, whose members control more than $1 trillion in assets—regarding this litigation. CalPERS and SBA, who are both members of the Council, informed ADM that major shareholders would object to the proposal as inadequate and unfair to ADM shareholders, for the reasons stated in this memorandum. ADM has ignored these objections and

instead has pressed forward for Court approval of the proposed Settlement. *See* Declaration of Ann L. Yerger ("Yerger Decl.") ¶¶ 9, 10.

* * * *

Respectfully submitted,

/s/ Mark C. Hansen
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Attorneys for
California Public Employees Retirement Systems, Inc. and the Florida State Board of Administration

Date: July 2, 1997

ADDENDUM C

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

Case No. 95-2279

Honorable Harold A. Baker
Judge Presiding

PAUL FELZEN, TRUSTEE OF LOUISE LASKIN TRUST—1991 and SANDRA ESNER,
Plaintiffs,
v.
DWAYNE O. ANDREAS, *et al.*,
Defendants,
and
ARCHER DANIELS MIDLAND COMPANY,
a Delaware Corporation,
Nominal Defendant.

IN THE COURT OF CHANCERY
OF THE STATE OF DELAWARE
IN AND FOR NEW CASTLE COUNTY

Consolidated C.A. No. 14403

IN RE: ARCHER DANIELS MIDLAND COMPANY

DECLARATION OF ANN L. YERGER

Ann L. Yerger hereby declares pursuant to 28 U.S.C. § 1746:

1. I am over eighteen years of age and have personal knowledge of the matters stated herein.

2. I am currently employed by the Council of Institutional Investor's [*sic*] (the "Council") as director of the Council's research service. The Council is located at 1730 Rhode Island Avenue, Suite 512, Washington, D.C. 20036. The Council is an association of more than 100 public corporate and union pension funds, with more than $1 trillion in assets. I have been employed by the Council since January 1996. Prior to that I was employed for five years by the Investor Responsibility Research Center as Deputy Director of the Center's Corporate Governance Service.

3. On November 5, 1996, Jacob A. Goldberg of the law firm Spector & Roseman, P.C., called me at the Council of Institutional Investors to describe the Archer Daniels Midland Company derivative litigation. I discussed Council members' ongoing concerns about the independence of ADM's board of directors.

4. About a month later, Mr. Goldberg phoned to set up a meeting with the Council. In response to my request for a written summary of the lawsuit, he mailed a letter dated December 15, 1996 to the Council's offices. A true and correct copy of this letter is attached hereto as Exh. A.

5. In this letter, Mr. Goldberg stressed that the firm was interested in meeting with the Council and Council members to discuss "the troublesome systemic problems plaguing the ADM Board of Directors." Exh. A at 1. A primary goal of plaintiffs' lawsuit, according to Mr. Goldberg, was to "recover for ADM as much of the wasted $190 million as is reasonably and realistically pos-

sible from the culpable officers and directors." *Id.* at 2. Equally important, he continued, were "the structural problems with ADM's board." *Id.* Goldberg stated that "any resolution of this case requires us to seek various fundamental changes to the ADM board, its structure and the way [it] governs ADM." *Id.*

6. On December 19, a Council staffer spoke with Mr. Goldberg and Robert M. Roseman of Spector & Roseman, P.C. The Council forwarded its Bill of Rights and definition of "independent" director to the law firm of Spector & Roseman, P.C.

7. That was the Council's last substantive conversation about the lawsuit with counsel for plaintiffs. On May 30, a reporter from the *Wall Street Journal* called me to discuss the proposed settlement. Shortly thereafter, on June 3, an irate individual shareholder faxed a copy of the proposed settlement to the Council.

8. I analyzed the proposed settlement and determined that it makes no meaningful improvement in ADM's corporate governance, and, in my opinion, is not in the best interest of ADM or its shareholders. Most importantly, the proposed settlement's definition of "outside" (or independent) director falls significantly short of the Council's definition. While purportedly modeled after the Council's standard, the proposed settlement's definition added undefined "materiality" hurdles to various categories of "outside" directors that falsely classify "inside" directors as "outside" directors.

9. I immediately contacted Mr. Roseman to explain the Council's concerns with the proposed settlement definition and to clarify the impact of the materiality hurdles. In response to my criticism of the proposed definition, Mr. Roseman told me that ADM refused to accept the Council's more stringent definition of "outside" director. He explained that, under the Council's definition, the company

would be forced to remove certain directors from its board.

10. I asked Mr. Roseman to provide a written analysis of ADM's board using the proposed definition. Mr. Roseman's response is attached hereto as Exh. B. According to Mr. Roseman's analysis, the only ADM directors who do not qualify as "outside" directors are company chairman Dwayne Andreas, CEO G. Allen Andreas and Shreve Archer, father of ADM's treasurer. All of the remaining 10 board members qualify as "outside" directors under the proposed settlement's definition, even though four directors—two attorneys whose law firms provide legal services to the company, and two executives of companies or their affiliates that do business with ADM—have ongoing business relationships with ADM and accordingly are beholden to management. These four directors do not qualify as independent "outside" directors under the Council's definition or any other generally accepted standard of true independence.

11. ADM has been a poster child for the corporate governance movement for years. The settlement of this derivative action offers an unprecedented opportunity to implement changes in ADM's bylaws that will benefit ADM and its shareholders. This opportunity should not be squandered.

12. I do not believe that the proposed settlement is fair, reasonable, adequate, or in the best interest of ADM and its shareholders. Indeed, I do not believe that the proposed settlement offers any significant benefit to ADM or its shareholders.

I declare under penalty of perjury that the foregoing is true and correct.

Dated this 2d day of July, 1997.

/s/ Ann L. Yerger
ANN L. YERGER

[Notarization and Exhibits Omitted in Printing]

ADDENDUM D

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

Case No. 95-2279

Honorable Harold A. Baker
Judge Presiding

PAUL FELZEN, TRUSTEE OF LOUISE LASKIN TRUST—1991 and SANDRA ESNER,
Plaintiffs,
v.
DWAYNE O. ANDREAS, *et al.*,
Defendants,
and
ARCHER DANIELS MIDLAND COMPANY,
a Delaware Corporation,
Nominal Defendant.

IN THE COURT OF CHANCERY
OF THE STATE OF DELAWARE
IN AND FOR NEW CASTLE COUNTY

Consolidated C.A. No. 14403

IN RE: ARCHER DANIELS MIDLAND COMPANY

DECLARATION OF SARAH A.B. TESLIK

Sarah A.B. Teslik hereby declares pursuant to 28 U.S.C. § 1746:

1. I am over eighteen years of age and have personal knowledge of the matters stated herein.

2. I have been the Executive Director, attorney and principal staffer for the Council of Institutional Investors (the "Council") since its formation in 1985. The Council is a non-profit association of corporate, public and Taft-Hartley pension funds that addresses investment issues. Council members invest over a trillion dollars on behalf of millions of employees and beneficiaries. Objectors California Public Employees' Retirement System and the Florida State Board of Administration are members of the Council.

3. The Council is a very deliberate and cautious organization that only adopts policies on essentially unanimous votes, and only after careful research and discussion. The Council has adopted fewer than a dozen corporate governance policies in all of its years of existence. Each of these has been so basic that every one of the Council's corporate members has voted in favor of each of the policies put up to them for a vote, and most of the policies are standard operating procedure at most or many of the nation's largest companies.

4. The first and probably the most central of the Council's policies is its requirement that a majority of a corporation's directors be independent from potentially compromising financial, familial or professional relationships to the company. The Council defines independence for these purposes in a detailed definition which, in essence, defines a director as independent if his or her only non-trivial connection to the board is his or her board seat. Members adopted this definition after they agreed that a board was much less likely to perform properly its central

function as an independent oversight body if most of its individual members were not, in fact, independent. Without this foundation policy, members felt most other corporate governance standards and procedures were meaningless. The policy and definition were adopted with unanimous votes on April 5, 1991. A copy of this policy is attached hereto as Exhibit "A".

5. The other central policy of the Council is its position on confidential voting. Directors, of course, are elected by shareholders, and so the election process is the vital link that provides meaningful accountability to shareholders. When this policy was debated, members agreed unanimously that this link is weakened, threatened, or shattered if those who run for office count their own ballots. That is an election practice that members did not believe would be tolerated in any other part of American life and should not be tolerated in corporate elections either.

6. The Council therefore on June 23, 1989 unanimously adopted a policy, attached hereto as Exhibit "B", supporting a confidential ballot—supporting the idea, in other words, that neutral third parties selected by the corporation should count shareholders' proxies. With increasing numbers of employee and institutional service provider shareholders who could suffer retribution if they dared to cast votes against management, members believed that this policy would only become more important over time.

7. The Council's majority standard for board independence is so universally accepted that it is the standard now used by nearly 85 percent (84.7 percent) of S&P 500 companies. Indeed Council data indicate that only 17 companies of the 483 member of the S&P 500 surveyed by the Council have fewer independent directors than ADM.

8. In the proposed settlement ADM offers an independence standard and definition that are, in my opinion (a) completely meaningless because of clever modifying language; (b) virtually identical to changes already proposed by the company more than a year ago, and without reference to the derivative lawsuit; (c) worse (less protective of shareholders) than the standards already in place at all but 15 percent of S&P 500 companies; and (d) so completely dated in language as to be archaic.

9. The proposed settlement provides that directors will be deemed to be "outside" even if they have personal, business, or professional ties to the company and/or its senior management, unless the relationship is deemed by the company to be "*material to the company or to the director.*" With a company the size of ADM, I cannot imagine a single relationship any one person could ever have, personal, professional, or otherwise, to ADM that would be material *to ADM*. This standard is therefore, in my opinion, a standard that virtually no director can fail. And yet it was Council members' belief that even the smallest of financial or personal relationships can genuinely affect a person's independence because of its potential to affect *the person*.

10. The company offers this can't-fail-to-be-met standard despite the fact that the widely accepted Council standard was already submitted to it by two of its largest shareholders, and two of the largest Council members—the California Public Employees' Retirement System and the Florida State Board of Administration—and received an exceptionally high endorsement of 41.6 percent of voting shareholders at the company's October 17, 1996 annual meeting.

11. The offer in the proposed settlement that direct management representation on the board will be limited to no more than three seats was lifted almost verbatim from the *Governance Committee Report to the Board of Directors of Archer Daniels Midland Company* (Jan. 15,

1996), which is attached hereto as Exhibit "C". This Committee was established and acted prior to the filing of the lawsuit to which this proposed settlement is the proposed conclusion. The ADM board adopted all of the recommendations in the Report. *See* Exhibit "E". So shareholders gain nothing from this proposed settlement they did not already have. And they did not have anything innovative here in any event: according to Council data, this company suggestion is standard operating procedure at most S&P 500 companies anyway—86.5 percent have three or fewer executives on the board.

12. Similarly the concept of a "lead director" seems to me to be another essential repeat of a change already called for in the 1996 Report, with the renaming of the lead director as the vice chairman. A similar repackaging appears to have occurred with the settlement's proposal to establish a governance committee to assess board and committee effectiveness. Under current board policies the nominating committee is responsible for annual director "self-assessment and board evaluation," while all nonmanagement directors handle the "establishment and performance criteria for evaluation of the CEO." As a result, the creation of this separate corporate governance committee does not appear to represent any meaningful innovation from current company practice.

13. The proposed settlement's requirement that separate nominating, compensation and audit committees must be composed exclusively of outside directors was also lifted verbatim from the 1996 Report.

14. The proposed settlement does offer a version of confidential voting that was not contained in the Report. But it is, if anything, an even more meaningless provision, in my opinion, than the definition of independence used for directors. The proposed settlement indicates the company will grant shareholders confidential voting—but only, it seems, in those situations in which it is irrelevant —only in situations where there are no proxy contests or

solicitations. In these situations the proposed settlement indicates there will *not* be confidential voting. And, although it seems nearly irrelevant under the circumstances, the company also does not indicate whether in those trivial and routine situations in which votes will be tallied confidentially, the confidentiality will last only until the polls are closed or whether it is permanent. Other companies with confidential voting policies generally, in the Council's experience, make this clear—it is a distinction that matters a great deal, especially to individual employee shareholders.

15. I have compared the governance provisions of the proposed settlement with the provisions already accepted by the board in the 1996 Report. This comparison is summarized in Exhibit "D" hereto. In my opinion, the few items in the settlement that cannot be found in the Report are trivial and provide no benefit to shareholders. On balance, the proposed settlement is no improvement over the governance provisions already accepted in the Report. I am unable, therefore, to identify new, positive, and meaningful corporate governance changes offered in the proposed settlement. This is particularly surprising and disappointing since I personally, numerous Council members individually, and other members of Council staff repeatedly made offers to ADM directors, consultants and other representatives to provide information on independent directors and other core member and Council policies that could have formed the basis of a very limited and conservative but meaningful set of governance principles.

16. Since the proposed governance provisions offer nothing significantly new, the proposed settlement provides no value to ADM or to its shareholders. However, a *truly* independent board could add significant value. A recent study by the McKinsey & Co. consulting firm found that 50 money managers representing $850 billion in assets were willing to pay an 11 percent "good governance" premium. A discussion of this study is attached hereto as Exhibit "F".

I declare under penalty of perjury that the foregoing is true and correct.

Dated this 2d day of July, 1997.

/s/ Sarah A.B. Teslik
SARAH A.B. TESLIK

[Notarization and Exhibits A-E Omitted in Printing]

EXHIBIT F TO TESLIK DECLARATION

THE WALL STREET JOURNAL, MONDAY, JUNE 30, 1997

WHY INVESTORS PUSH FOR STRONG CORPORATE BOARDS

Manager's Journal
By Jennifer H. van Heeckeren

Trustees and staff of the California Public Employees' Retirement System are developing guidelines to grade companies in Calpers's portfolio on the independence of their boards. Calpers cannot be ignored: Its $80 billion in equities make it one of the nation's largest shareholders and a force to be reckoned with in the governance arena. A study I conducted with Diane Del Guercio at the University of Oregon shows that Calpers has the power to provoke significant change, such as takeover attempts, turnover, restructurings and asset sales.

CEOs would be wise to embrace the idea of strongly independent boards. For if investors can't get boards to work well, they may turn to other measures—sitting on boards themselves, lobbying for direct government regulation or supporting a return of corporate raiders.

The growing power and independence of boards reflects a reversal of a trend that dates to the early years of this century. A seminal event occurred in 1914, when repre-

sentatives of J.P. Morgan resigned from 30 company boards in a single day. They and other institutional investors had held sway in boardrooms for more than two decades, leaving CEOs with little real decision-making power. But as they came under critical public and political scrutiny, they beat a hasty retreat. Family owners were also losing influence, as founders aged and ownership tilted toward outsiders. So a new group of professional CEOs, bred in new management schools, took the reins of corporate America.

Their grip loosened in the 1950s, when an economic boom drove a wave of investors into stocks. Increased individual ownership heightened expectations and fed a belief in shareholder democracy. New regulations requiring the disclosure of senior-management pay, along with the rise of the corporate raider, spurred a growing number of contested elections for boards, known as proxy contests. After a concerted lobbying and publicity effort on governance issues by the Business Roundtable, new regulations in 1956 clamped down on proxy battles, and CEOs prevailed at the end of the decade.

Today institutional investment is again booming. After declining to as low as 15% in the 1940s, institutional ownership returned to turn-of-the-century levels of 50% and higher in the mid-1980s. Takeovers flourished in the '80s environment of few regulatory restrictions and easy financing via junk bonds. But public opinion turned against raiders, state regulations and court decisions made takeovers more difficult, junk bonds dried up, and management created innovative takeover defenses. Many CEOs believed they had won the governance battle.

CEOs who resist pressure for strong governance risk having Calpers or regulatory bureaucrats tell them what kind of board they should have.

But institutional investors looked for other ways to prod CEOs. In 1992 the Securities and Exchange Commission made it easier for investors to coordinate on governance issues. Shareholders issued "hit lists" of underperforming companies, announced shareholder proposals and communicated directly with management. But it didn't make sense for Calpers and other institutions to intervene in each of the thousands of companies whose stock they held. They have turned to boards—shareholders' elected representatives—as management watchdogs.

What do these investors want? The bottom line is long-term returns. The most active investors are pension funds with mind-boggling obligations. Calpers will need to be able to pay out $30 billion each year to its beneficiaries by 2020. Institutional investors rely on strong, independent boards to create shareholder value. They believe strong boards will help companies correct mistakes, recover from crises, and find, support and reward outstanding CEOs.

Numerous recent examples, along with academic research, support the notion that boards can have a significant impact on stock prices. Recent research by McKinsey in conjunction with Institutional Investor found that many large private money managers—especially those looking for long term value—are willing to pay a higher stock price for companies with good, independent board governance. We surveyed 50 money managers representing about $850 billion in assets, and found that they were willing to pay an 11% good-governance premium on average.

How should CEOs respond to the demand for strong, independent boards? Well-performing companies have the option of doing nothing for now—but only until there is a period of poor results, a complex acquisition, or a crisis. CEOs could search for ways to thwart investors, as they did in the 1980s. But underlying forces make this strategy unpromising. Institutional ownership will probably con-

tinue to increase. Public opinion is suspicious of CEOs, whose pay has dramatically increased while companies downsized. The most prominent investors, meanwhile, are more sympathetic—not the "greedy raiders" of the '80s, but institutions like Calpers, which pays the pensions of firemen, police officers and school librarians. Politicians aren't likely to attack these investors on behalf of CEOs. Finally, the SEC has been embracing a pro-shareholder stance that seems unlikely to change.

CEOs can benefit personally from strong, independent boards. As major stockholders themselves, they should pursue strategies that increase the stock price. Harmonious relations with investors enable CEOs to focus their time and energy on substantive business issues. CEOs will find, too, that investors are much more patient and understanding in bad times if they trust the board. And while a weak board may rubber-stamp the CEO's decisions when times are good, often its first response to a crisis is to fire the CEO—whereas a strong board with substantive knowledge of strategy and company performance will tend to support management.

CEOs who resist pressure for strong governance risk having Calpers or regulatory bureaucrats tell them what kind of board they should have—an outcome that serves no one's interest. After all, the best boards aren't built by outsiders. Only the CEO has the knowledge and the position to build the optimal board for his company. Rather than fight the tides, CEOs should take the lead by tailoring strong boards for their companies, and thereby shape the next era of corporate governance to their—and their shareholders'—benefit.

Ms. van Heeckeren is a consultant in McKinsey & Co.'s Cleveland Office. Robert Felton, a McKinsey partner, contributed to this article.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1997

California Public Employees' Retirement System and Florida State Board of Administration,

Petitioners,

v.

Paul Felzen, et al.,

Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

BRIEF FOR RESPONDENTS IN OPPOSITION

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QUESTIONS PRESENTED

Neither of the questions presented in the petition for writ of certiorari is an accurate or fair statement of any issue involved in this case. The proper statement of the issues presented is:

1. Whether a nonparty shareholder, who objects to the settlement of a derivative action, but does not move to intervene in the district court, must be allowed to appeal the district court's approval of the settlement.

2. Whether a nonparty who ignores a prior decision of the court of appeals holding that only parties or those who seek to intervene have a right to appeal from a district court's orders is entitled to relief from that rule simply because the court of appeals' prior decision arose out of a different factual situation.

TABLE OF CONTENTS

PAGE

QUESTIONS PRESENTED i

TABLE OF AUTHORITIES iii

STATEMENT OF THE CASE 1

REASONS FOR DENYING THE PETITION 5

I. The Petition Should Be Denied Because It Presents An Inaccurate Statement Of The Decision Below And Asks This Court To Review Issues Not Presented In This Case 5

II. The Petition Should Be Denied Because The Decision Below Does Not Create A Conflict With Any Circuit Over A Matter Of Sufficient Importance To Require This Court's Resolution 8

III. There Is No Issue Of Retroactivity In This Case That Justifies Review By This Court 15

CONCLUSION 16

APPENDIX ..... *infra*

TABLE OF AUTHORITIES

Cases PAGE(S)

Bell Atlantic Corp. v. Bolger, 2 F.3d 1304 (3d Cir. 1993) 8

Carlough v. Amchem Products, Inc., 5 F.3d 707 (3d Cir. 1993) 8

Croyden Associates v. Alleco, Inc., 969 F.2d 675 (8th Cir. 1992), *cert. denied*, 507 U.S. 908 (1993) 8

Daily Income Fund, Inc. v. Fox, 464 U.S. 523 (1984) 11

Gottlieb v. Wiles, 11 F.3d 1004 (10th Cir. 1993) 8

Guthrie v. Evans, 815 F.2d 626 (11th Cir. 1987) 8

In re Brand Name Prescription Drugs Antitrust Litigation, 115 F.3d 456 (7th Cir. 1997) ..... *passim*

In re General Tire & Rubber Co. Sec. Litig., 726 F.2d 1075 (6th Cir.), *cert. denied*, 469 U.S. 858 (1984) 11, 12

In re VMS Limited Partnership Securities Litigation, 976 F.2d 362 (7th Cir. 1992) ... 3, 12, 15

Layne & Bowler Corp. v. Western Well Works, Inc., 261 U.S. 387 (1923) 10

Loran v. Furr's/Bishop's Inc.,
988 F.2d 554 (5th Cir. 1993) 8

Marino v. Ortiz,
484 U.S. 301 (1988) ..... *passim*

PaineWebber Inc. Ltd. Partnerships Litig.,
94 F.3d 49 (2d Cir. 1996) 9

Papilsky v. Berndt,
466 F.2d 251 (2d Cir.), *cert. denied*,
409 U.S. 1977 (1972) 11

Research Corp. v. Asgrow Seed Co.,
425 F.2d 1059 (7th Cir. 1970) 7

Rosenbaum v. MacAllister,
64 F.3d 1439 (10th Cir. 1995) 8, 9

Sanyo Manufacturing Corp. v.
International Union Electronic,
69 F.3d 541 (8th Cir. 1995) 8

Shults v. Champion,
35 F.3d 1056 (6th Cir. 1994) 8

Smith v. Sperling,
354 U.S. 91 (1957) 13

Tryforos v. Icarian Dev. Co.,
518 F.2d 1258 (7th Cir. 1975),
cert. denied, 423 U.S. 1091 (1976) 7

Court Rules

Fed. R. App. P. 3(c) 9, 10, 12

Fed. R. Civ. P. 23 12

Fed. R. Civ. P. 23.1 ..... 4, 10, 11, 12

STATEMENT OF THE CASE

Respondents Paul Felzen and Sandra Esner are Archer Daniels Midland Company ("ADM") shareholders who brought this derivative action in July 1995 on behalf of ADM and its shareholders against 17 ADM directors who had been board members during a period in which ADM had engaged in illegal price-fixing. In May 1997, after two years of discovery and extensive negotiations,[1] the parties agreed to settle the case on the basis of defendants' commitments, designed to strengthen the independence of ADM's Board of Directors and prevent illegal conduct by the Company in the future, to restructure ADM's Board of Directors, to revise the structure and responsibilities of key Committees of ADM's Board and to pay $8 million, part of which ADM would use to fund an independent oversight committee for legal compliance.[2] On July 7, 1997, the

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[1] During the two years this litigation was pending, counsel for respondents reviewed all the documents ADM produced for various civil litigations, briefed successive motions to dismiss and consulted with corporate governance experts and ADM's largest institutional investors, including petitioner CalPERS, all to the end of developing measures for ADM's Board to adopt to improve corporate governance and to assure independence of the Board as part of a settlement of the litigation. On May 30, 1997, the district court entered an order preliminarily approving the proposed settlement and directing that notice be mailed to ADM's shareholders of the proposed settlement and hearing to consider whether the proposed settlement was fair, reasonable and adequate. The notice was mailed to more than 243,000 ADM shareholders.

[2] The $8 million payment is to come from the defendants' Directors and Officers liability insurance—a $10 million policy containing exclusions that put in issue whether there would be any coverage for this action.

district court held a hearing to consider the proposed settlement and the fee petition submitted by respondents' counsel relating to the services they had performed in the case and the benefits conferred on the corporation.

Petitioners, two ADM shareholders who represent less than one percent of the Company's shareholders, first appeared in the case at the July 1997 hearing. Although petitioners did not seek to intervene in this case, they participated fully in the hearing, objecting to both the settlement and the fee request filed by respondents' counsel. After a four-hour hearing, the district court rejected the objections, approved the settlement as fair, reasonable and adequate and, with some modifications to the fee requested by respondents' counsel in their fee petition, awarded counsel fees.

At no time before, during or after the July hearing did petitioners seek to become parties to the proceedings before the district court. Instead, one week after the district court rejected their position, petitioners filed a notice of appeal to the Court of Appeals for the Seventh Circuit as nonparties. Petitioners adopted this course of action notwithstanding the fact that six weeks previously, on May 30, 1997, the Seventh Circuit issued its opinion in *In re Brand Name Prescription Drugs Antitrust Litigation*, 115 F.3d 456 (7th Cir. 1997), squarely holding that nonparties who have not sought to become parties by moving to intervene may not appeal from district court orders. The *Brand Name Drugs* case was a class action, but the court of appeals' decision in that case was not limited to class actions. Instead, the court based its decision principally upon this Court's decision

in *Marino v. Ortiz*, 484 U.S. 301 (1988)—an employment discrimination case that was not a class action.

The Seventh Circuit acknowledged that its decision in *Brand Name Drugs* was somewhat at variance with some of its previous decisions. It held, however, that "[a]lthough some cases have allowed nonparties to appeal without first intervening in the district court, this bypass is no longer permissible after *Marino*." 115 F.3d at 457. Moreover, the *Brand Name Drugs* court pointed out that the Seventh Circuit had already abandoned the practice of condoning appeals by nonparties several years earlier in its decision in *In re VMS Limited Partnership Securities Litigation*, 976 F.2d 362 (7th Cir. 1992).

In *Brand Name Drugs*, the Seventh Circuit clearly delineated the procedure that nonparty objectors who wish to appeal from a district court order must follow. An objector must move to intervene in the district court. If the district court grants the motion, the objector can, of course, appeal. If the district court denies the motion to intervene, the objector may appeal from the denial. *Brand Name Drugs*, 115 F.3d at 458. The rule in the Seventh Circuit—in effect since that court's 1992 decision in *VMS*, 976 F.2d 362, and plain beyond any doubt since the *Brand Name Drugs* holding—has been and remains that a nonparty who wishes to appeal from a district court order must seek to become a party by moving to intervene.[3]

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[3] The *Brand Name Drugs* case involved separate appeals by class members who had opted out of the class and sought to appeal from the district court's order granting summary judg-

(continued...)

When petitioners filed their objections to the settlement and fee petition in this case, the *Brand Name Drugs* decision was the most recent—and most authoritative—statement of the procedures that nonparties seeking to appeal in the Seventh Circuit from an order of a district court would have to follow. When petitioners attempted to proceed without following the procedures laid out in that opinion, respondents moved to dismiss their appeal. The court of appeals granted respondents' motion, holding that shareholders in derivative suits, like other nonparties, were required to follow the procedures set out in *Marino* and *Brand Name Drugs*.

In their petition for writ of certiorari, petitioners totally misrepresent the status of the law of the Seventh Circuit at the time they decided to appeal as nonparties without seeking to intervene. They do not even mention the *Brand Name Drugs* decision. Nor do they mention the Seventh Circuit's holding that its previous decisions permitting nonparty appeals "can no longer be considered authoritative, in light of *VMS*." 115 F.3d at 458.

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[3] (...continued)
ment in favor of the wholesaler defendants and nonparty class members who had appeared at the fairness hearing to object to the settlement but who had not intervened. Although the *Brand Name Drugs* decision does not on its face distinguish between the two orders appealed from, the appeal numbers which the Seventh Circuit's ruling dismissed include three appeals by class members from the July 1, 1996 final order of the district court approving the settlement (Nos. 96-2813, 96-2878, 96-2904). The court below failed to make this distinction, but it made no difference because it recognized that the distinction is "inconsequential." Appendix to the Petition for a Writ of Certiorari, hereinafter "___a", at 4.

On the basis of their misrepresentation as to the status of the law, petitioners seek to portray themselves as victims of a change in the law that they did not and could not anticipate. And they ask this Court to assist them by granting them the right to appeal as nonparties despite their failure, or refusal, to comply with the clear procedural requirements applicable to all cases in the Seventh Circuit. There is no reason for this Court to exercise its discretionary jurisdiction to protect petitioners from the consequences of decisions for which they alone are, and should be, responsible.

REASONS FOR DENYING THE PETITION

I. The Petition Should Be Denied Because It Presents An Inaccurate Statement Of The Decision Below And Asks This Court To Review Issues Not Presented In This Case.

The Petition mischaracterizes the decision of the court below by representing that it requires that a nonparty be formally made a party to the litigation as a prerequisite to the right to appeal.

That is an erroneous characterization of the decision of the court below, which simply applied to petitioners this Court's decision in *Marino* and its own holding in *Brand Name Drugs* requiring that nonparties move to intervene:

> Only parties may appeal. So too with shareholders, who have no more right to speak for the firm or control its litigation decisions than bondholders or banks or landlords, all of whom have contractual interests that may be affected by

> litigation. It may be, as appellants stress, that some district judges would not be receptive to attempts to intervene for the purpose of appeal, but the Supreme Court spoke to this in *Marino* when observing that a denial of a motion to intervene is itself appealable. 3a.

Thus, the issue in this case is not, as petitioners argue, whether objectors need to be formally made parties, but rather, whether objectors who wish to preserve the right to appeal must move to intervene. If objectors move to intervene and their motion is denied, they may appeal that denial and argue to the court of appeals why they should be allowed to intervene, that is, why their interests are not adequately represented by the existing parties. To the extent some district courts have discretion in ruling on motions to intervene, their discretion is still subject to review. Petitioners, therefore, are wrong in arguing that the ability to appeal "turns on a purely discretionary decision by the trial court." (Petition at 13.) The ability to appeal turns on the simple procedure of moving to intervene.

The Petition also seeks review by claiming that the decision of the court below was applied retroactively. The issue petitioners pose is premised solely on a statement of the status of Seventh Circuit law at the time the district court issued its orders in this case that completely ignores the recent holding in *In re Brand Name Prescription Drugs*, 115 F.3d 456. In *Brand Name Drugs*, the court of appeals removed any doubt that the Seventh Circuit would follow this Court's opinion in *Marino* requiring that nonparties who wish to preserve the right to appeal must first seek to intervene. In *Brand Name Drugs*, the Seventh Circuit also plainly

stated that "any contrary implication" of pre-*Marino* decisions, such as *Research Corp. v. Asgrow Seed Co.*, 425 F.2d 1059 (7th Cir. 1970), "can no longer be considered authoritative." *Id.* at 458. In the face of this plain statement of the law, petitioners sought to excuse their failure to make a motion to intervene by claiming that they relied on *Research Corp. v. Asgrow Seed Co.* 7a.[4] If petitioners relied on a decision that was "no longer authoritative" they have only themselves to blame. They certainly have no basis to argue that, in dismissing the appeal, the court below applied a new jurisdictional rule to them when the court of appeals simply applied pre-existing Seventh Circuit law.

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[4] Petitioners also claim to have relied on a 22-year-old footnote in *Tryforos v. Icarian Dev. Co.*, 518 F.2d 1258 (7th Cir. 1975), *cert. denied*, 423 U.S. 1091 (1976). However, in the docketing statement they filed with the Seventh Circuit in July 1997 they did not cite *Tryforos*. In any event, as the court below pointed out, the *Tryforos* footnote was not reliable authority—it did not analyze the question of whether nonparty shareholders to a Rule 23.1 action may appeal—and was not settled precedent in light of the intervening decision of this Court in *Marino v. Ortiz*:

> Footnote 22 in *Tryforos* cites one case from the 1940s that permits such appeals, but that opinion did not give reasons. (*Tryforos* also cites one district court opinion from the 1960s, an odd reference for a rule of appellate jurisdiction.) An unexplained practice does not offer shelter from a later opinion of the Supreme Court holding that only parties may appeal, and withdrawing from the appellate courts any exception-making power. 3a.

Although noting that petitioners "tell us" they relied on *Asgrow Seed* and *Tryforos* (7a), the court below did not, as petitioners represent, "acknowledge" that, in failing to seek to intervene, petitioners had followed all proper procedures under settled Seventh Circuit law at the time they appealed. (Petition at 9.)

II. The Petition Should Be Denied Because The Decision Below Does Not Create A Conflict With Any Circuit Over A Matter Of Sufficient Importance To Require This Court's Resolution.

Petitioners seek review of the Seventh Circuit's requirement that a nonparty file a petition for leave to intervene as a condition to the right to appeal, principally on the ground that the Third Circuit follows a different rule. *See Bell Atlantic Corp. v. Bolger*, 2 F.3d 1304 (3d Cir. 1993); *Carlough v. Amchem Products, Inc.*, 5 F.3d 707 (3d Cir. 1993). These decisions do not remotely justify this Court's review of this case.[5]

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[5] All other circuits that have squarely addressed the issue since *Marino* have held that nonparties in class actions must seek to intervene if they want to appeal from an order approving a settlement. *Guthrie v. Evans*, 815 F.2d 626 (11th Cir. 1987); *Croyden Associates v. Alleco, Inc.*, 969 F.2d 675 (8th Cir. 1992), *cert. denied*, 507 U.S. 908 (1993); *Sanyo Manufacturing Corp. v. International Union Electronic*, 69 F.3d 541 (8th Cir. 1995); *Loran v. Furr's/Bishop's Inc.*, 988 F.2d 554 (5th Cir. 1993); *Shults v. Champion*, 35 F.3d 1056 (6th Cir. 1994); *Gottlieb v. Wiles*, 11 F.3d 1004 (10th Cir. 1993). As the citations indicate, this Court previously denied certiorari in one case, *Croyden Associates v. Alleco, Inc.*, *supra*, in which the court of appeals reached the same conclusion as the Seventh Circuit in this case. No circuit, other than the Third, has held that nonparties in derivative actions may appeal orders approving settlements without seeking to intervene. The Tenth Circuit did not, as petitioners state, "adopt" *Bell Atlantic*. (Petition at 13.) To the contrary, in *Gottlieb v. Wiles*, *supra*, the court held that unnamed class members who had not intervened could not appeal. In *dicta*, the court noted that *Bell Atlantic* was inapposite to a class action settlement because it involved a derivative settlement. Other cases that petitioners cite as having held that nonparties need not seek to intervene in these circumstances do not squarely address the issue or pre-date *Marino*. In *Rosenbaum v. MacAllister*, 64

(continued...)

In the first place, even if the different procedure adopted by the Third Circuit were viewed as creating the kind of conflict among the circuits that might merit resolution by this Court, review of this case is not warranted. The decision in this case is plainly correct and is supported by a well-reasoned opinion. Indeed, as this Court held in *Marino*, the rule requiring a petition to intervene as a condition to any appeal is fully justified by the language of Rule 3(c) of the Federal Rules of Appellate Procedure. Review here would only further delay full implementation of the structural changes in ADM's Board of Directors and legal compliance that the settlement was designed to effectuate.[6]

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[5] (...continued)
F.3d 1439, 1442 (10th Cir. 1995), the court concluded that intervention was not required because the appeal sought review of the award of attorneys' fees and expenses, not the settlement between the parties. In *PaineWebber Inc. Ltd. Partnerships Litig.*, 94 F.3d 49 (2d Cir. 1996), the court dismissed an interlocutory appeal from the district court's order denying a motion to intervene on the grounds that the motion was solely in aid of a motion that was both interlocutory and outside the collateral order exception.

[6] Respondents' expert Professor John C. Coffee of Columbia University School of Law described the corporate governance measures ADM had agreed to implement as "state of the art" and the new legal compliance provisions as being "of special value" to ADM. Respondents' financial expert R. Alan Miller of Philadelphia Investment Banking Company opined that ADM shareholders stand to gain $158 million or more from implementation of the settlement. Although petitioners now complain that the settlement did not involve a greater cash payment, during the settlement negotiations, they, and other institutional investors, emphasized that they sought corporate governance reforms, not a monetary recovery, for ADM's shareholders.

Secondly, and perhaps more fundamentally, the suggestion that a conflict requiring the attention of this Court arises every time that there is a difference among the circuits in what is essentially a procedure is clearly unsound. Petitioners have not offered any valid reason why it is essential or urgent that this Court resolve the difference. *See, e.g., Layne & Bowler Corp. v. Western Well Works, Inc.*, 261 U.S. 387, 393 (1923) (Court will not grant writ of certiorari except in cases where the conflict "is a real and embarrassing conflict of opinion and authority between the circuit courts of appeal.") As with other procedural rules that ultimately affect a court's jurisdiction (these may be as basic as due dates and filing fees), parties or those who wish to be parties are on notice—or have a responsibility to know—of appellate court rules, and can adjust their conduct accordingly.

Petitioners argue that some courts have allowed nonparties to appeal in other circumstances and criticize the court below for its "single-minded reliance on *Marino*." (Petition at 19.) This argument ignores that *Marino* is the applicable law and that the court below explained at great length the reasons for adhering to *Marino* and Fed. R. App. P. 3(c) in this case. It also begs the issue because petitioners provide no sound reason for carving out an exception to *Marino* and Rule 3(c) for nonparties in derivative actions. The intervention requirement does not eliminate any procedural right. It does not undermine the purposes of Fed. R. Civ. P. 23.1.

The fact that Rule 23.1 requires that every shareholder receive a court-approved notice of a dismissal or proposed settlement of a derivative action does not remotely suggest that they have an automatic right to

appeal. To the contrary, Rule 23.1 recognizes that shareholders should be afforded the opportunity to make their case to the district court, which is entrusted with the task of approving a settlement.[7] The Seventh Circuit's procedure in no way reduces a shareholder's ability to participate in the settlement approval process under Rule 23.1 or increases the burden on shareholders who wish to do so. These shareholders still have the option to object without seeking to intervene. They simply may not appeal if they fail to move to intervene. Other than their disagreement with the result the district court reached in this case, petitioners do not suggest, nor could they, that they were not afforded a full and fair hearing in the district court.

Petitioners' suggestion that parties will choose to sue in circuits that require an objector to intervene to achieve a collusive settlement is nonsensical and insulting to the federal judiciary. This assumes that a district court judge will rubber-stamp a "collusive settlement" in the face of cogent, well-founded objections and deny a well-founded motion to intervene by an objector who wishes to appeal and further that a court of appeals will not carefully review the district court's denial. If this is truly the situation, then it would make no difference if a nonparty could appeal without seeking to intervene. In either case, its appeal would be futile.[8]

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[7] The cases petitioners cite make this clear. *See, e.g., Daily Income Fund, Inc. v. Fox*, 464 U.S. 523 (1984); *Papilsky v. Berndt*, 466 F.2d 251 (2d Cir.), *cert. denied*, 409 U.S. 1977 (1972), and cases cited, Petition at 14-15 n. 18.

[8] Petitioners suggest that a court of appeals will not review a district court's denial of a motion to intervene, citing *In re*

(continued...)

As the Seventh Circuit explained in *Brand Name Drugs*, 115 F.3d at 457-58, there are sound reasons for a court of appeals to require nonparties to intervene:

> [A]s for the class members . . . who want to appeal even though they are not named plaintiffs, to allow them to appeal would be an even worse affront to intelligent judicial administration because it would fragment the control of the class action. . . . If class members can file their own appeals, the coherence of the class is destroyed, the scope of the class action becomes unclear, and the control over the action becomes divided and confused. So they may not appeal. *In re VMS Limited Partnership Securities Litigation*, 976 F.2d 362 (7th Cir. 1992).

The court below recognized that these reasons apply as well to shareholder derivative actions, and that neither *Marino* nor Rule 3(c) provides any basis for distinguishing between Rule 23 and 23.1 nonparties. 4a. Indeed, the court below reasoned that there are stronger reasons for requiring shareholders to become parties if they want to appeal an order because, in a derivative action,

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[8] (...continued)
General Tire & Rubber Co. Sec. Litig., 726 F.2d 1075, 1087 (6th Cir.), *cert. denied*, 469 U.S. 858 (1984). Petition at 14 n. 13. In that case, the court affirmed the district court's denial of the objectors' motion to intervene because they sought solely to oppose the district court's approval of a derivative settlement and the court of appeals affirmed the approval of the settlement over the objectors' arguments. There is certainly nothing untoward in the court's conclusion that the objecting shareholders' interests, that is the interests of the corporation and all the shareholders, were "adequately protected" by a fair, reasonable and adequate settlement.

an individual investor is not an injured party and has no individual right to sue:

> A derivative suit is brought by an investor in the corporation's (not the investor's) right to recover for injury to the corporation. . . . Stockholders may *replace* the board if dissatisfied with its performance, but they may not *displace* the board in litigation. So it cannot be surprising that stockholders other than the named plaintiffs are not treated as parties in derivative litigation—their citizenship is ignored when determining diversity, see *Smith v. Sperling*, 354 U.S. 91, 77 S.Ct. 1112, 1 L.E.2d 1205 (1957), and they are not allowed to opt out. Corporate management may affect the interests of stockholders without notifying them or obtaining their consent; by investing in stock, they placed their funds at the management's disposal and obtained, in exchange, the right to choose future managers. Shareholders have no more the attributes of parties when managers settle derivative litigation than when managers settle antitrust litigation.

5a. (Emphasis in original)

The decision of the court below necessarily follows from the fact that a shareholder in a derivative suit is pursuing corporate, not individual, rights. If a shareholder wants to proceed on behalf of the corporation in court, it must become a party and must adequately and fairly represent the interests of all shareholders in enforcing the corporation's rights. If a shareholder seeks only to appeal from a district court order, as in the case of an objector, it must at least seek to intervene.

Intervention is not a complex procedure or one that unduly burdens a shareholder who wishes to appeal

from a district court's order approving a settlement or dismissing a case.[9] Certainly in this case the filing of a motion to intervene presented no obstacle to petitioners, whose lawyers traveled to Illinois to participate in a lengthy hearing. On the other hand, if an objector is unwilling to intervene to become a party with some stake in the litigation and some responsibility to the corporation—even if only as a party objector—it is unfair to allow this individual shareholder to "hold up" the corporation and its remaining shareholders.

Petitioners' overblown rhetoric that requiring a shareholder to seek to intervene has serious implications rests on faulty premises. It falsely assumes that intervention imposes any real burden and interferes with any existing rights of a shareholder. It does not. Shareholders have no right to sue individually on claims of injury to the corporation. They may be allowed to do so on behalf of a corporation only if the corporation's managers agree or the court permits them to bring a derivative action. Requiring them to move to intervene is consistent with that scheme.

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[9] Petitioners argue that objectors who intervene to appeal the approval of a settlement face discovery (Petition at 16), but the court below never suggested that an objector had to become the representative party in the litigation. To the contrary, *Marino* and the court below make clear that the objector may, if it wants, intervene solely for the limited purpose of appeal. 3a, 6a.

III. There Is No Issue Of Retroactivity In This Case That Justifies Review By This Court.

The decision of the court below discusses at length the issue of whether a new appellate ruling involving the jurisdiction of the appellate court should be applied retroactively. As already noted, this entire discussion is gratuitous in this case because the rule applied here had already been announced by the Seventh Circuit in *VMS* and had been forcefully reiterated and again applied six weeks prior to the filing of the notice of appeal in this case in *Brand Name Drugs*. Petitioners nonetheless attempt to justify issuance of a writ of certiorari on this additional ground, arguing that the discussion of the court below creates a conflict among the circuits and that the decision to apply the ruling here retroactively "wrongly insulates from appellate scrutiny a plainly collusive settlement in one of the most significant shareholder derivative suits." (Petition at 23.)

This entire argument is beside the point because this case involves no new jurisdictional requirement. The conflict among the circuits to which the court below refers exists in this case only at the level of dictum because it pertains to a situation inapplicable to this case. And the suggestion of a collusive settlement is a fabrication—raised in and flatly rejected by the district court—for which there is not the slightest basis in the record.[10]

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[10] Indeed, petitioners' counsel admitted at the July 7, 1997 hearing in the district court that he had no evidence of any collusion (Transcript of Proceedings ("Tr.") at 62) and the district court made an express finding that there was no basis for any claim of collusion: "I find no basis for claims of collu-

(continued...)

What appears to be involved here is an effort by petitioners' counsel to divert attention from, and to avoid the consequences of, their own mishandling of this case in the district court. They could and should have filed a petition for leave to intervene. Indeed, in light of the *Brand Name Drugs* decision, their failure to do so is incomprehensible; but it is certainly not reason for this Court to involve itself in a matter that is a non-issue in this case.

CONCLUSION

For the foregoing reasons, this Court should deny the Petition for Writ of Certiorari.

May 22, 1998

Respectfully submitted,

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[10] (...continued)
sion. Just none. These people have dealt with each other professionally and at arm's length. . . ." (Tr. at 82). The relevant pages of the hearing transcript are contained in an Appendix to this Brief.

APPENDIX

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF ILLINOIS
URBANA DIVISION

PAUL FELZEN, et al.,	)	
	)	
Plaintiffs,	)	
v.	)	Case No.: 95-2279
	)	
	)	
DWAYNE O. ANDREAS, et al.,	)	
	)	
Defendants.	)	

REPORT OF PROCEEDINGS

DATE: July 7, 1997
FAIRNESS HEARING
BEFORE: HAROLD A. BAKER
Judge Presiding

APPEARANCES:

For the Plaintiff: (NOTE APPEARANCES ON PAGE 2)

For the Defendants: (NOTE APPEARANCES ON PAGE 2)

Toni M. Judd
U.S. Court Reporter
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significance of the largest corporate fiasco in recent memory with, according to their own experts, Mr. Miller, 250 million in losses to the company wrapped up.

Eight million, Your Honor, means this. Lawyers get money. I don't believe I am misstating that, Your Honor. Because under the terms of the settlement, which is what I am focusing on for a moment, here is what was provided. There will be an eight million dollar pot, but half of it plus interest is agreed to go to the lawyers. Now they have asked for less in their fee petition, but the agreement itself talks about half of the eight million dollars being set aside for the plaintiffs' lawyers.

Which, Your Honor, when we spoke of collusion earlier I realize that's an ugly word and I realize that sounds very pejorative. I make no pejorative aspersions. I don't know what happened in the settlement process. I don't mean to say that I did.

But I can tell your honor that what we cited to the court and the cases says the following. Where there is a cash settlement and a large percentage of the cash is earmarked for lawyers, that by itself raises an inference of collusion.

In fact, their opening commentator, Mr. Coffee says as much in some of his law review work. Now as I say, I wasn't there. I don't know. But where you see a

of cumulative voting was Joseph Medell, the publisher of the "Chicago Tribune," and had Mr. Joseph Medell been alive today, I would have had his affidavit saying he would like to see that cumulative voting be part of the bylaws of Archer Daniels, as part of the governance.

I brought along a book out of my library to show you that cumulative voting isn't just up in Mars with the Pathfinder. A book entitled, "Cumulative Voting for Directors," written by Charles M. Williams, published by the Harvard Business School, it's 200 pages talking about cumulative voting for directors. And to say that in part of their negotiations this shouting and all of this didn't take into the fact cumulative voting, I fail to see that they should receive the severance, the compensation that they are asking for. And actually what I believe the basis is for my discussion, my objection on the fees paid. Thank you.

THE COURT: All right. The court's ready to rule. Having heard the remarks of the proponents of the settlement and the remarks of those in opposition, the court concludes that the settlement, which is before the court is fair, reasonable, and adequate. The court considers the strength of the plaintiffs' claims in the case as balanced against what was obtained in the settlement.

The case the plaintiffs had was not, as one of my colleagues described, "another case as a dead bang winner." Far from it. There were serious questions raised in the motion to dismiss, and I tried to look back through the record to see what discovery wasn't afforded and I think that pool of documents was available, and I can remember discussions with counsel in this case and in the other civil ADM cases that were pending about the availability of the document pool that had been created by Judges, Shadur, Mihm, and I don't know about the Judge in California participating in that, but I believe all of that information was available to the plaintiffs in the case.

So that the record really is slightly misleading as far as discovery is concerned because the plaintiffs did have all of that information available to them.

In addition, the parties, as you see from the docket, got to the point where they were squabbling about compelling discovery and having a hearing on the motion to dismiss, and the defendants kept asking to advance the hearing on the motion to dismiss, and then they began negotiations in the case and the court abstained from hearing or ruling on the motion at the request of the parties so that they could talk to each other.

Well, because lawyers talk to each other doesn't mean that the lawyers are in collusion. Far from it. Of

course, quite obviously they have to communicate and talk if they are going to find some alternative means of settling their disputes other than going to judgment in a court of law.

The defendants' ability to pay. There is a ten million dollar cap on the insurance. Mr. Hansen suggests that the directors had deep pockets. I have been in the legal profession and the litigation end of it for over forty years, I am sorry to say, and I wonder if he has ever tried to pursue a suit for transferring assets in fraud of creditors. That needs a good deal of luck.

And to assume that those directors are holding all of their assets, I think is an unwarranted assumption, so that the ten million dollars is a realistic sum to think was available; at least it was readily available—obviously available.

The complexity, length, and expense of further litigation also has to be considered. This case would have gone on for years. I wouldn't have had to suffer through it, being a senior judge somebody else could have taken it over, by my guess would be five years of further litigation.

The amount of opposition to the settlement. That's been commented upon by the proponents of the settlement. While the objections I am sure are heartfelt

and sincere, they really represent a very very small percentage of the shareholders of the corporation. The [sic] Not that the objections aren't to be discounted just because they are small—from a small number, relatively small number of shareholders, but still the overwhelming reaction to the proposed settlement has been acceptance.

I had no idea Edward Dessen was going to appear. I have known him for years. He is a businessman. He owns property. He is a very outspoken person, and, true, with faint praise, he approved the settlement. He may be reflective of the way a large percentage of shareholders feel. Well, it's a start. It's a beginning.

I find no basis for claims of collusion. Just none. These people have dealt with each other professionally and at arm's length as far as the progress of the case has been concerned.

Certainly competent counsel with experience has expressed support for the settlement. I have to respect that. And I have already spoken a little bit about the stage of the proceedings and the amount of discovery. The case has goon on for two years. A great deal—a substantial portion of which has been devoted to attempting to finding an alternative to the settlement of the dispute.

And, the document pool that was created through Judge Mihm, and I have blocked his name, Milt Shadur was

available to the parties of the plaintiff.

I rely on what Professor Coffee has said and what Alan Miller, the statements made by Miller in support. I respect them as experts. As Professor Coffee observed, it's a state of the art far from perfect, far from being ideal, but still represents a great step forward in corporate governance.

So, in conclusion, I find that the settlement is fair, reasonable, and adequate and I will proceed to hearing this afternoon at 1:30 on the question of fees and allocation of the funds that are sought there.

Supreme Court, U.S.
FILED
AUG 4 1998
CLERK

No. 97-1732

IN THE
Supreme Court of the United States
OCTOBER TERM, 1997

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM and FLORIDA STATE BOARD OF ADMINISTRATION,
Petitioners,

v.

PAUL FELZEN, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

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PETITIONERS' REPLY BRIEF TO OPPOSITIONS OF ARCHER DANIELS MIDLAND COMPANY AND DIRECTORS OF ARCHER DANIELS MIDLAND COMPANY

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TABLE OF AUTHORITIES

Cases	Page
Bayard v. Lombard, 50 U.S. (9 How.) 530 (1850)	6
Bell Atlantic Corp. v. Bolger, 2 F.3d 1304 (3d Cir. 1993)	*passim*
Budinich v. Becton Dickinson & Co., 486 U.S. 196 (1998)	10
Carlough v. Amchem Prods., Inc., 5 F.3d 707 (3d Cir. 1993)	2, 7
Christianson v. Colt, 486 U.S. 800 (1988)	10
Ex parte Cockcroft, 104 U.S. 578 (1882)	6
Croyden Assocs. v. Alleco, Inc., 969 F.2d 675 (9th Cir. 1992)	2
George v. Camacho, 119 F.3d 1393 (9th Cir. 1997)	8, 9, 10
Gottlieb v. Wiles, 11 F.3d 1004 (10th Cir. 1993)	2
Kircher v. May, 484 U.S. 72 (1987)	6
Ex parte Leaf Tobacco Bd. of Trade, 222 U.S. 578 (1911)	6
Marino v. Ortiz, 484 U.S. 301 (1988)	*passim*
New York v. Reebok Int'l Ltd., 96 F.3d 44 (2d Cir. 1996)	3
Northern Pipeline Constr. Co. v. Marathon Pipe Line Co., 458 U.S. 50 (1982)	9
Paine Webber Inc. Ltd. Partnerships Litig., In re, 94 F.3d 49 (2d Cir. 1996)	2
Prettyjohn v. Shalala, 23 F.3d 1572 (10th Cir. 1994)	9
Rosenbaum v. MacAllister, 64 F.3d 1439 (10th Cir. 1995)	2, 8
Shults v. Champion Int'l Corp., 35 F.3d 1056 (6th Cir. 1994)	2, 7
Snyder v. Smith, 736 F.2d 409 (7th Cir. 1984)	9
Tryforos v. Icarian Dev. Co., 518 F.2d 1258 (7th Cir. 1975), *cert. denied*, 423 U.S. 1091 (1976)	10
United States ex rel. Louisiana v. Boarman, 244 U.S. 397 (1917)	6, 7
Walker v. City of Mesquite, 858 F.2d 626 (11th Cir. 1987)	2

TABLE OF AUTHORITIES—Continued

Rules	Page
Fed. R. App. P. Rule 3(c)	1, 3, 6, 8
Fed. R. Civ. P.	
Rule 23	2, 3
Rule 23.1	2, 3, 5
Rule 26(a)	4
Other Materials	
Timothy A. Duffy, *The Appealability of Class Action Settlements by Unnamed Parties*, 60 U. Chi. L. Rev. 933 (1993)	8
5 James W. Moore, *Moore's Federal Practice* (3d ed. 1988)	8
Charles A. Wright, *et al.*, *Federal Practice and Procedure*:	
Vol. 7C (Supp. 1988)	8
Vol. 15A (2d ed. 1992)	7

Respondents Archer Daniels Midland Company ("ADM") and Directors of ADM ("Directors") do not deny that this case presents an irreconcilable circuit split over nonparty shareholder appeals. Nor do they challenge the importance of the issue to the appellate rights of an entire class of litigants and the judiciary's ability to police collusive derivative suit settlements. Pet. 13-17. ADM and the Directors simply defend the Seventh Circuit's result. But even they ultimately abandon its reasoning, conceding that neither *Marino v. Ortiz*, 484 U.S. 301 (1988), nor Fed. R. App. P. 3(c), bars all nonparty appeals. Point 3, *infra*.

ADM and the Directors likewise do not and cannot seriously dispute that this case raises a second, distinct split with the Ninth Circuit over whether courts reversing settled jurisdictional precedents have the power to consider prospective application of their decisions. Pet. 23-25. They do not dispute the importance of this issue. Pet. 25-26. And, again, they do not and cannot defend the Seventh Circuit's reasoning, seeking instead to defend its result primarily on alternative grounds. Point 4, *infra*.

1. Unable to contest that the circuits *do* disagree over nonparty shareholder appeals, ADM rests its opposition on the panglossian assertion that the split is sure to resolve itself at some (unspecified) future date. ADM Opp. 8-14. But such wishful thinking is no basis for ignoring a split the parties and lower courts concede is real and live—only an invitation for perpetuating confusion among the courts of appeals and uncertainty for litigants. Besides, ADM provides no factual basis for its speculation.

First, not one of the cases ADM cites as evidence of supposed impending resolution involves a shareholder appeal under Rule 23.1. Instead, each involves the separate circuit split over the propriety of nonparty Rule 23 class action appeals. *See* ADM Opp. 8 (citing cases). The Rule 23 split, however, is not presented by this petition (*see* Pet. i, Question Presented 1), and lower courts have suggested that the case for nonparty appeals is analytically

different—and stronger—for Rule 23.1 shareholders than for Rule 23 class members.[1]

Second, even if developments in the Rule 23 class action split had some bearing on certiorari in this case, ADM's assurances of resolution are demonstrably incorrect. Within the last five years, the Second, Third, and Sixth Circuits have issued post-*Marino* decisions reaffirming the right of nonparty class action litigants to appeal.[2] In fact, contrary to ADM's express representation, the most recent circuit decision to address the issue found the split so nettlesome that to avoid controversy and protect its decision from certiorari it assumed without deciding that non-

[1] *See Gottlieb v. Wiles*, 11 F.3d 1004, 1011 (10th Cir. 1993) (McKay, C.J.) (citing *Bell Atlantic* and arguing that case for Rule 23.1 nonparty appeals is stronger for three reasons: because "[u]nlike class actions under Rule 23, in shareholder derivative suits under Rule 23.1, a preliminary affirmative determination that the named plaintiffs will fairly and adequately represent the interest of other class members is not a prerequisite"; "there is no opt-out provision in shareholder derivative suits. Thus, all shareholders are bound by the outcome regardless of their objections"; and "one of the risks peculiar to shareholder derivative actions is that [p]laintiffs' attorneys and the defendants may settle in a manner adverse to the interests of the plaintiffs by exchanging a low settlement for high fees") (citations omitted). *See also Rosenbaum v. MacAllister*, 64 F.3d 1439, 1442 (10th Cir. 1995) ("[i]ndeed, the decision [*Gottlieb*], by its analysis distinguishing shareholders' derivative suits and *Bell Atlantic Corp. v. Bolger*, 2 F.3d 1304 (3d Cir. 1993), might be read to support Russell's standing to appeal the derivative suit portion of the settlement agreement").

[2] *See* Pet. 12 n.10, citing *Shults v. Champion Int'l Corp.*, 35 F.3d 1056, 1061 (6th Cir. 1994) (expressly considering *Marino* and holding that it "addressed the standing to appeal of non-parties and not . . . of non-representative members of a class or derivative suit" and thus does not overrule caselaw permitting certain nonparty class member appeals); *In re PaineWebber Inc. Ltd. Partnerships Litig.*, 94 F.3d 49, 53 (2d Cir. 1996) (even though motion to intervene denied, nonparty class members may appeal final judgment); *Carlough v. Amchem Prods., Inc.*, 5 F.3d 707, 713-14 (3d Cir. 1993) (upholding class member's right to appeal and expressly rejecting *Croyden Assocs. v. Alleco, Inc.*, 969 F.2d 675 (9th Cir. 1992) and *Walker v. City of Mesquite*, 858 F.2d 626 (11th Cir. 1987), which had relied on *Marino* to forbid such appeals).

party class members can appeal. *New York v. Reebok Int'l Ltd.*, 96 F.3d 44, 48 (2d Cir. 1996) ("in view of the differences in the circuits on the issue of the appellate standing of unidentified class action members, we deem it advisable also to review the merits of appellants' claims"). That is hardly the mark of a split resolving itself.

ADM dwells on the fact that the Court previously denied petitions in two cases. ADM Opp. 9-11. But both cases were Rule 23 class actions; ADM fails to cite a single post-*Marino* Rule 23.1 petition considered by the Court, and petitioners are aware of none. Both of the class action cases ADM cites were, moreover, obviously poor vehicles for resolving even that distinct split. By the time *Weinberg v. Croyden Associates* reached the Court, both respondents had entered bankruptcy and, thus, any opinion rendered by the Court would have had no binding impact on the parties to that case. *See* Brief in Opposition at 23-25 (No. 92-613, filed Dec. 23, 1992). In *Ridgeway v. Pfizer, Inc.* (where petitioners twice sought review), respondents devoted an entire section of their brief to arguing "THE UNIQUE AND UNUSUAL FACTS OF THIS CASE MAKE IT UNSUITABLE FOR REVIEW BY THIS COURT," noting among other things that the class members seeking review had attempted to challenge the settlement only after affirmatively choosing to accept (and apparently failing to repudiate) its benefits. *See* Briefs in Opposition at 11-12 (Nos. 93-1912 and 94-843, filed July 1, 1994, and Dec. 8, 1994).

Third, if ADM *were* correct that the lower courts are gradually coming to conclude that *Marino* bars Rule 23.1 nonparty shareholder appeals, that would only further underscore the need for the Court to correct a serious misunderstanding of its brief and largely unexplained *per curiam* precedent. Indeed, even ADM and the Directors *concede*—in conflict with *Marino*'s dicta and the Seventh Circuit's holding—that *Marino* and Fed. R. App. P. 3(c) do not bar all nonparty appeals. *See* Point 3, *infra*.

2. Respondents do not (and cannot) contest that at stake in the Rule 23.1 split is whether an entire class of

persons have a right to appeal or may do so only with the discretionary concurrence of the trial court. Pet. 13-17. Nor do (or can) they dispute that the quality of justice administered by federal courts in derivative litigation is directly implicated: requiring shareholders to assume the costs and burdens of parties will decrease the likelihood of their participation and increase the opportunities for improper and collusive settlements to evade judicial detection. Pet. 14-15; *Bell Atlantic*, 2 F.3d at 1310.[3]

Instead, ADM responds only that "gigantic organizations like petitioners" can afford to become parties. ADM Opp. 16. But obviously not all dissident shareholders have petitioners' resources; if petitioners' resources are relevant at all to the question of certiorari, they weigh in favor of granting review.[4] Nor can respondents seriously dispute that even large institutional shareholders often find prohibitive the costs and burdens of becoming a party in modern commercial litigation (including submission to often unlimited depositions, compliance with Rule 26(a), and other discovery demands). *See* Remarks of District Judge Vaughn R. Walker, ABA National Securities Litigation Institute, June 5, 1998.[5] Nor do respondents have any meaningful response to the fact that, even for shareholders willing and able to assume such burdens, current law in the Seventh Circuit and elsewhere strongly disfavors intervention where (as in Rule 23.1 practice) the motion to intervene comes after a tentative settlement is reached. Pet. 16 & n.18; *id.* at 7 n.7.[6]

3. ADM and the Directors spend much of their briefs arguing the correctness of the Seventh Circuit's intervention mandate. *See* ADM Opp. 14-18; Directors Opp. 13-19. But such merits arguments only underscore the deep disagreement over nonparty shareholder appeals requiring this Court's attention.

Tellingly, too, while ADM and the Directors defend the Seventh Circuit's result, they abandon its reasoning. Confronted by overwhelming evidence that nonparty appeals are routine (Pet. 20-21), ADM and the Directors frankly concede that at least some nonparty appeals *are* permissible. *See* ADM Opp. 14 n.6; Directors Opp. 17. This admission is in direct conflict with *Marino*'s dicta and the Seventh Circuit's holding that "only parties may appeal." Pet. App. 3a; 484 U.S. at 304. Nor do (or can) respondents harmonize their endorsement of some

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[3] ADM and the Directors likewise offer no rejoinder to the fact that leaving this split unresolved leaves shareholder litigants uncertain of their appellate rights and the procedures they need to follow (Pet. 16), and encourages forum shopping (Pet. 17).

[4] Unlike many dissident shareholders, petitioners have the financial wherewithal to provide merits briefs and oral argument comparable to those provided by respondents' able counsel. Moreover, petitioners have used their resources to contact a number of other institutional investors who have authorized petitioners to inform the Court that they stand ready to provide *amici* filings should the Court grant review. These include the Colorado Public Employees' Retirement Association, Louisiana State Employees' Retirement System, Massachusetts Pension Reserves Investment Management Board, Missouri State Employees' Retirement System, New Jersey Division of Investment, New York City pension funds, New York State Common Retirement Fund, United Food and Commercial Workers International Union Staff Trust Fund, and State of Wisconsin Investment Board.

[5] "[I]nstances of institutional investors actively leading a [securities class] litigation effort remain relatively rare. . . . This is no surprise. As Professors Weiss and Beckerman recognized, institutional investors have disincentives to becoming [parties]. . . . Lawsuits are costly in time, money and other resources." *Id.* at 7-8. After touting petitioners' supposed resources, respondents ironically go on to malign petitioners for using them to promote corporate governance standards (*see* Directors Opp. 6; ADM Opp. 16) aimed at preventing a repeat of the ADM fiasco where the company has admitted multiple acts of criminal wrongdoing (Pet. 4) and top officials are currently in the middle of a federal criminal trial.

[6] Respondents purport to assure the Court that intervention will not be a problem. *See* ADM Opp. 16; Directors Opp. 14-15 & n.2. But they cite no cases to support their assurances. And they do not dispute that the Seventh, Second, and Fifth Circuits strongly disfavor post-settlement intervention. Respondents are left only to offer sheer speculation that courts will (sometime) in the future create a special exception for shareholder litigants.

nonparty appeals with the Seventh Circuit's reading of Fed. R. App. P. 3(c) as restricting appellate jurisdiction to formal parties. *See* Pet. 22-23; Pet. App. 2a, 3a.

ADM and the Directors attempt to limit their retreat by suggesting that only nonparties "personally addressed" by trial court orders may appeal. *See* ADM Opp. 14 n.6; Directors Opp. 17. But neither *Marino* nor the Seventh Circuit ever suggested such a rule, and respondents fail to cite any court that has. Indeed, their proffered rule is inconsistent with common law practice permitting unnamed class members to appeal (Pet. 18); with this Court's longstanding jurisprudence allowing *all* "priv[ies] to the record" to appeal (Pet. 19); *United States ex rel. Louisiana v. Boarman*, 244 U.S. 397 (1917)[7]; and with federal appellate practice which has routinely permitted unnamed privy nonparty appeals. *See, e.g.*, Pet. 21 & n.24 (citing cases where unnamed persons legally liable to reimburse defendant for amounts paid in judgment were permitted to appeal); Pet. 21 & n.23 (citing cases where unnamed attorneys were permitted to appeal trial court orders denying a fee request made by a party). *See also* 15A Charles A. Wright, *et al., Federal Practice and Procedure* § 3902.1, at 122 (2d ed. 1992) (named nonparty presents "easiest" but not exclusive case for appeal); *id.* at 126 (though order does not "bind a nonparty by name," he may appeal when order has "[o]bvious and important effects" on him). Even if respondents' rule had some

[7] ADM cites *Ex parte Leaf Tobacco Bd. of Trade*, 222 U.S. 578, 581 (1911) and *Karcher v. May*, 484 U.S. 72, 77 (1987) for the proposition that only parties may appeal. ADM Opp. 14. But ADM itself inconsistently admits that at least some nonparties can appeal. And neither case suggests otherwise. *Id.* 14 n.6. Besides, *Louisiana* explained that *Ex parte Leaf Tobacco Bd. of Trade* stands only for the proposition that parties *and* nonparty privies may appeal. 244 U.S. at 402. And *Karcher* expressly acknowledged that one who is a party "or has . . . been treated as a party" may appeal. 484 U.S. at 77. *See also, e.g., Bayard v. Lombard*, 50 U.S. (9 How.) 530, 551 (1850) (parties and privies may appeal); *Ex parte Cockcroft*, 104 U.S. 578, 579 (1882) (actual parties or ones "treated as such" by trial court may appeal).

basis in law rather than in their imagination, they fail to explain how it would forbid appeals by shareholders who, like petitioners, had their objections personally and specifically overruled by the trial court.[8]

ADM and the Directors repeatedly denigrate the Third Circuit's decision in *Bell Atlantic* as poorly reasoned. *See, e.g.*, ADM Opp. 8; Directors Opp. 11. Yet they never confront the Third Circuit's holding that *Marino* barred only complete strangers (white police officers) from attacking a settlement between plaintiff class members (black officers) and the defendant (police administration), and did not involve the appellate rights of class members themselves. 2 F.3d at 1308 n.6; Pet. 19. They fail to note that, unlike the Seventh Circuit's decision, *Bell Atlantic's* reading of *Marino* is consistent with this Court's prior holding in *Louisiana* and other cases, common law practice, and regular federal decisions permitting nonparty privy appeals. They fail to inform the Court that *Bell Atlantic* has been approvingly cited twice by the Tenth Circuit (*see supra* note 1); that the Third Circuit has subsequently acknowledged its continuing conflict with other circuits and unflinchingly adhered to its own view (*see Carlough*, 5 F.3d 707); that its reasoning was subsequently adopted by the Sixth Circuit in the class action context (*see Shults*, 35 F.3d at 1056); or that commentators have repeatedly endorsed its view.[9] Meanwhile, re-

[8] *See* Hearing Tr. at 79 ("All right. The court's ready to rule. Having heard the remarks of the proponents of the settlement and the remarks of those in opposition [*i.e.*, petitioners], the court concludes that the settlement, which is before the court is fair, reasonable, and adequate.").

[9] ADM tries to twist Wright & Miller's acknowledgment that "it has been ruled" by some courts that shareholders must intervene into support for those decisions. ADM Opp. 15. But Wright & Miller's view could not be more clear that, despite *Marino*, "[t]he justification for recognizing appeal standing in some of these [nonparty] cases is so compelling as to justifying putting aside any formal requirement of intervention, although the 'better practice' is to seek intervention in the district court." 15A Wright, *et al., supra*, § 3902.1, at 122 (quoting *Marino*, 484 U.S. at 303). ADM is

spondents are unwilling (and unable) to defend the Seventh Circuit's alternative reading of *Marino* and Fed. R. App. P. 3(c) as barring all nonparty appeals.[10]

4. Respondents label *George v. Camacho*, 119 F.3d 1391 (9th Cir. 1997) (*en banc*) a "peculiar" decision and assert it was based on "extremely unusual facts." *See* ADM Opp. 19; Directors Opp. 21. But perjoratives aside, they can hardly deny the existence of a split: the Ninth Circuit in *George* held that courts have the power

similarly incorrect when it represents that "the only authority" Wright & Miller cites in support of its endorsement of nonparty shareholder appeal is a "pre-*Marino*" decision. *Compare* ADM Opp. 15 *with* 7C Wright, *supra*, § 1839 n.22 (Supp. 1998) (expressly relying on *Bell Atlantic*). ADM is incorrect yet again when it states that the only post-*Marino* cases Moore cites in favor of nonparty shareholder appeals are from the Third Circuit; in fact, Moore also cites the Tenth Circuit's decision in *Rosenbaum*. 5 J. Moore, *Moore's Federal Practice* § 23.1.10[3] n.36 (3d ed. 1998). ADM's citation to Kaplan, *Continuing Work of the Civil Committee: 1966 Amendments of the Federal Rules of Civil Procedure (I)*, 81 Harv. L. Rev. 356, 392 n.137 (1967) deals exclusively with Rule 23 class members and states only that by objecting class members do not automatically become parties; it is silent as to their appellate rights as nonparty objectors. ADM Opp. 16 n.10. And ADM does not even attempt to respond to *The Appealability of Class Action Settlements by Unnamed Parties*, 60 U. Chi. L. Rev. 933, 946 (1993), cited favorably by the Seventh Circuit below (Pet. App. 2a), which expressly endorses petitioners' (and *Bell Atlantic*'s) view of *Marino*.

[10] ADM fleetingly attempts to defend the Seventh Circuit's decision on the alternative ground that the appellate courts will be overburdened if nonparty shareholders were allowed to appeal. ADM Opp. 18 n.12. But this merits argument only underscores ADM's disagreement with courts (like the Third Circuit) that stress the importance of shareholder participation to preventing and exposing improper settlements. 2 F.3d at 1310. Besides, nonparty shareholder appeals have been routinely heard for decades in the Seventh Circuit and elsewhere without incident; ADM cites no court or judge complaining of undue burden, nor a single commentator on the subject. In fact, the only "evidence" ADM can muster from decades of practice permitting nonparty shareholder appeals is citation to a single dispute, and even that case involved a Rule 23 class action, not a shareholder appeal.

to consider overruling existing jurisdictional precedents only prospectively (2 F.3d at 1398); the Seventh Circuit below held that they do not (Pet. App. 7a-8a, 10a). The Seventh Circuit expressly acknowledged its "disagree-[ment]" with *George* on this score; stated that its opinion "was circulated before release to all judges in active service" because it "creates a conflict among the circuits" (Pet. App. 10a); and "overrule[d]" its own precedent, *Snyder v. Smith*, 736 F.2d 409, 415 (7th Cir. 1984), because it had previously "reached the same conclusion" as *George*. Pet. App. 8a.[11]

Respondents do not attempt to contest petitioners' explanation of the importance of the interests at stake in the split. Pet. 26. ADM does not even attempt to defend the correctness of the panel's decision below; the Directors' attempts to do so at best underscore the depth of their disagreement with the Ninth Circuit, and at worst are simply incoherent.[12] In the end, ADM and the Direc-

[11] *Cf. Prettyjohn v. Shalala*, 23 F.3d 1572, 1575 (10th Cir. 1994) (like Ninth Circuit, holding over dissent that court has power to consider prospective adjudication).

[12] The Directors assert that the court of appeals lacked adjudicatory power to hear petitioners because they were not parties. Directors Opp. 23 (court requires "'adjudicatory power' over Petitioners . . . as parties"). But this claim is literally incoherent given the Directors' own admission that courts of appeals do possess the power to hear at least some nonparty appeals. *Id.* 17 (conceding circuit courts may hear appeals from "order[s] formally addressed to a nonparty"). The Directors explain *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982), on the grounds that it permitted prospectivity in a jurisdictional dispute "only to avoid inequitable results." Directors Opp. 24. But this does nothing to insulate the court of appeals' assertion that it was *powerless* to consider inequitable results in this case. Pet. App. 10a ("[e]quitable considerations are altogether irrelevant"). And still no respondent has addressed the Ninth Circuit's analysis that *Budinich v. Becton Dickinson & Co.*, 486 U.S. 196 (1988) and *Christianson v. Colt*, 486 U.S. 800 (1988), simply do not control where (as in *George* and here) the court announces a new rule of law, or effects a change in the law. Pet. 29-30.

tors seek to defend the Seventh Circuit primarily on alternative grounds—arguing that "even if" the Seventh Circuit had held itself empowered to consider pure prospectivity, it would have declined to exercise that power in this case because petitioners could have divined the court's intention to make intervention mandatory. ADM Opp. 20-21; Directors Opp. 22.

Respondents' speculation about how the Seventh Circuit would have balanced the equities in this case is utterly irrelevant. The only question presented in this petition is whether courts have the legal *power* to consider prospective application of jurisdictional decisions overruling prior precedent. Whether a court of appeals would choose to *exercise* such power in this particular case is a question of applying law to the facts that become relevant only upon remand to the Seventh Circuit. Besides, respondents can offer only sheer guesswork for their claim that a court of appeals would find the equities in this case insufficient to warrant prospectivity; the Seventh Circuit expressly declined to reach the question. *See* Pet. App. 10a (ending opinion after holding itself powerless to balance equities favoring prospective and retroactive adjudication). And, in fact, petitioners have several unanswered arguments favoring prospectivity to make on remand: before the decision below, the Seventh Circuit had directly held that a nonparty shareholder's right to appeal was "clear" (*Tryforos v. Icarian Dev. Co.*, 518 F.2d 1258, 1263 n.22 (7th Cir. 1975), *cert. denied*, 423 U.S. 1091 (1976)); the Third Circuit had written a post-*Marino* opinion only four years earlier reaffirming the Seventh Circuit's view; the Tenth Circuit had approvingly cited the Third Circuit's opinion (*see supra* note 1); not a single published post-*Marino* case existed refusing a nonparty shareholder appeal; and leading commentators had expressly endorsed the Third Circuit's analysis. *See also* Pet. Reply 2-4.

CONCLUSION

The petition for a writ of certiorari should be granted.

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No. 97-1732

IN THE
Supreme Court of the United States
OCTOBER TERM, 1997

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM and FLORIDA STATE BOARD OF ADMINISTRATION,
Petitioners,

v.

PAUL FELZEN, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

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PETITIONERS' REPLY BRIEF

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12 pp

TABLE OF AUTHORITIES

Cases	Page
Bell Atlantic Corp. v. Bolger, 2 F.3d 1304 (3d Cir. 1993)	4, 6, 8, 9
Carlisle v. United States, 517 U.S. 416 (1996)	6
Celotex Corp. v. Edwards, 511 U.S. 1105 (1994)	6
In re Brand Name Prescription Drugs Antitrust Litig., 115 F.3d 456 (7th Cir. 1997)	2, 3, 4
In re General Tire & Rubber Co. Security Litig., 726 F.2d 1075 (6th Cir.), *cert. denied*, 469 U.S. 858 (1984)	7
George v. Camacho, 119 F.3d 1393 (9th Cir. 1997)	2, 9, 10
Gottlieb v. Wiles, 11 F.3d 1004 (10th Cir. 1993)	8
Henderson v. United States, 517 U.S. 654 (1996)	5
Marino v. Ortiz, 484 U.S. 301 (1988)	2, 5, 8
Pavelic & LeFlore v. Marvel Entertainment Group, 493 U.S. 120 (1989)	6
Tryforos v. Icarian Dev. Co., 518 F.2d 1258 (7th Cir. 1975), *cert. denied*, 423 U.S. 1091 (1976)	3, 9
VMS Ltd. Partnership Sec. Litig., 976 F.2d 362 (7th Cir. 1992)	4

Rules

Fed. R. App. P. 3(c)	2, 5
Fed. R. Civ. P. 23	3, 9

Other Materials

Timothy A. Duffy, Note, *The Appealability of Class Action Settlements by Unnamed Parties*, 60 U. Chi. L. Rev. 933 (1993)	6
3B James W. Moore, *Moore's Federal Practice* (1993):	
¶¶ 23.1.24[3]; 23.80[5]	4
7C Charles A. Wright, *et al.*, *Federal Practice and Procedure* § 1839 (1986)	4

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PETITIONERS' REPLY BRIEF

Respondents in opposition [1] do not dispute the Seventh Circuit's conclusion that the lower "[c]ourts have disagreed for several decades" about whether nonparty shareholders "must intervene as parties in order to appeal." Pet. App. at 2a. They do not offer any means of reconciling this split of authority. They do not attempt to respond to petitioners' argument that the Seventh Circuit's decision

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[1] Only the two individual plaintiffs in this derivative action, whose attorneys are currently slated to receive a substantial portion of the settlement's proceeds, chose to file an opposition to petitioners' certiorari petition. Brief for Respondents in Opposition ("BIO") at 1. Archer Daniels Midland Company and the individual director defendants, though parties to the derivative settlement, have waived opposition. Certain other attorneys for plaintiffs below who themselves opposed the fee amounts granted to counsel for respondents also have waived opposition.

was based on a misreading of *Marino v. Ortiz*, 484 U.S. 301 (1988), and Federal Rule of Appellate Procedure 3(c). Pet. at 17-23.[2] Nor do they rebut petitioners' substantial showing that the Seventh Circuit's new rule imposes a substantial burden on shareholders who seek to contest improper or inadequate derivative suit settlements.[3]

Respondents likewise do not (and cannot) dispute that the court of appeals created a second, independent circuit split with the Ninth Circuit over whether new jurisdictional rules must always be applied retroactively. Pet. App. at 10a (conceding "disagreement" with *George v. Camacho*, 119 F.3d 1393 (9th Cir. 1997)). They do not dispute that the Seventh Circuit's position in this split undercuts the judiciary's interest in promoting reliance on settled law and will have the effect of barring the appeals of an entire class of litigants. Pet. at 25-26. And, again, they do not even purport to defend the merits of the Seventh Circuit's position in this split. *Id.* at 26-30.

1. Instead, respondents spend much of their opposition arguing that, in an opinion issued six weeks before the Rule 23.1 hearing in this case, *In re Brand Name Prescription Drugs Antitrust Litigation*, 115 F.3d 456 (7th Cir. 1997), the Seventh Circuit "removed any doubt" that shareholders must intervene to appeal. BIO at 6. But

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[2] Respondents characterize petitioners as representing "less than one percent of the Company's shareholders." BIO at 2. Their combined 4.6 million shares, however, currently represent an investment of nearly $90 million, making them among the largest shareholders of Archer Daniels Midland Company, which respondents themselves elsewhere admit. *Id.* at 1, n.1.

[3] Respondents suggest that "petitioners' counsel admitted . . . that he had no evidence of any collusion" in this case. BIO at 15, n.10. But, on the contrary, the sole page of the record respondents cite shows petitioners' counsel arguing that "[w]here there is a cash settlement and a large percentage of the cash is earmarked for lawyers, that by itself raises an inference of collusion. * * * In fact, their opening commentator, Mr. Coffee says as much in some of his law review work." BIO App. at 2.

even if this procedural history were accurate, it would only underscore the need for certiorari by confirming that the issue presented recurs regularly and the Seventh Circuit is unlikely to reverse course and resolve its split with the Third and Tenth Circuits on its own accord.

In any event, respondents' procedural history is at odds with the Seventh Circuit's own explanation. Judge Easterbrook himself described *In re Brand Name* as holding only that "a class member in an action under Fed. R. Civ. P. 23 who has not become a party may not appeal from an order granting summary judgment." Pet. App. at 2a. Nothing in Judge Easterbrook's opinion, or *In re Brand Name* itself, even remotely suggests that decision also mandated intervention for shareholders seeking to appeal derivative settlements. Indeed, had the panel in *In re Brand Name* decided that nonparty shareholders must intervene, it would have been required to overrule the Seventh Circuit's prior contrary decision in *Tryforos v. Icarian Dev. Co.*, 518 F.2d 1258 (7th Cir. 1975) (Stevens, J.), *cert. denied*, 423 U.S. 1091 (1976), and to circulate its opinion among the entire circuit or seek an *en banc* hearing. The panel in this case could not have declared that *it* was "overrul[ing] *Tryforos* to the extent it permits non-party shareholders to appeal in actions under Rule 23.1." Pet. App. at 6a-7a. It would have had no reason to indicate that *this* decision creates a conflict with the Third Circuit's decision in *Bell Atlantic*. *Id.* at 7a. It would have had no need to devote several pages of its opinion to the question whether "to defer the effect" (*id.*) of its "new precedent" (*id.* at 7a-8a). And it would have had no need to circulate its opinion among the entire court of appeals for review on the grounds that it "overrules some of our decisions." *Id.* at 10a.

Ultimately, respondents can criticize petitioners only for failing to *predict* the Seventh Circuit's decision here.[4] But

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[4] In a footnote, respondents question whether petitioners even relied on *Tryforos*. BIO at 7, n.4. But petitioners expressly did

failing to guess that a court of appeals might reverse its own longstanding precedent and create a circuit split is hardly grounds for denying certiorari. Nor was the Seventh Circuit's result so easy to foresee. When petitioners filed their appeal in this case, nonparty shareholder appeals had been expressly endorsed by the Third Circuit only four years earlier, *Bell Atlantic Corp. v. Bolger*, 2 F.3d 1304 (3d Cir. 1993), and uniformly praised by recognized authorities on civil procedure.[5] The panel in *In re Brand Name*, moreover, barred Rule 23 nonparty appeals only of summary judgment orders. It nowhere revealed any intent to reverse a prior panel decision—just five years old—that expressly reaffirmed the right of Rule 23 class members to appeal settlement decisions. *VMS Ltd. Partnership Sec. Litig.*, 976 F.2d 362, 367, 368 n.8 (7th Cir. 1992) ("*Research Corp.* still controls [the] issue," permitting standing for "an unnamed class member who appeals the approval of a consent decree").[6]

2. Judge Easterbrook went out of his way to highlight for this Court the Seventh Circuit's "disagree[ment] with

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so in their brief to the court of appeals, as the Seventh Circuit acknowledged. Pet. App. at 2a-3a ("two shareholders who have appealed from the district court's approval of a settlement in this derivative action ask us to apply *Tryforos*"). The court of appeals even considered whether it could "defer the effect" (*id.* at 7a) of its reversal of *Tryforos* out of equity to petitioners, concluding only that it was powerless to do so (*id.* at 7a-10a).

[5] *See, e.g.*, 3B James W. Moore, Moore's Federal Practice, ¶ 23.1.24[3] (1993) (objector's right to appeal derivative suit settlement); *id.* ¶ 23.80[5] (1993) ("[a] member of the class who appears in response to the court's notice . . . and objects to the dismissal or compromise has a right to appeal from an adverse final judgment although he did not become a formal party of record"); 7C Charles A. Wright, *et al.*, Federal Practice and Procedure § 1839, at 182 (2d ed. 1986) ("[a]n objector to the settlement may appeal the court's approval of the compromise").

[6] Even *In re Brand Name*'s limited holding in the Rule 23 context was far from stable: at the time petitioners entered this case, *In re Brand Name* was subject to a motion for reconsideration and was later amended twice by the court of appeals.

the conclusion of [the Third Circuit in] *Bell Atlantic*" (Pet. App. at 7a). Respondents do not dispute the existence of this split, but nonetheless claim the Court should deny certiorari because the Seventh Circuit's position "is plainly correct and is supported by a well-reasoned opinion." BIO at 9. Yet, one of the primary functions of this Court's certiorari jurisdiction is to resolve circuit splits over questions of federal law; whether the reasoning of the Seventh Circuit or that of the Third (and Tenth) Circuits ultimately proves persuasive is immaterial. Petitioners have, moreover, already amply demonstrated that the Seventh Circuit's decision is based upon flawed interpretations of *Marino* and Federal Rule of Appellate Procedure 3(c). Pet. at 17-23. Tellingly, respondents do not even *attempt* to confront this analysis in their opposition. *See* BIO at 9.

Instead, respondents claim that circuit splits over "procedural rules that ultimately affect a court's jurisdiction" are not worthy of this Court's review because litigants can simply "adjust their conduct" to comply with any circuit's particular view. BIO at 10. But this Court has few duties more important than ensuring consistency in the administration of justice in the federal courts. Permitting open disputes over the federal rules to linger without resolution simply because they are "procedural" invites balkanization of the federal judiciary, undermines the judiciary's interest in promoting reliance on uniform procedures, and allows lower courts to disregard with impunity policies set and approved by this Court and Congress. Unsurprisingly, respondents can cite no authority for the rule of review they posit, nor can they explain the innumerable cases in which the Court *has* reviewed disagreements over the proper interpretation of "procedural" rules.[7]

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[7] *See, e.g., Henderson v. United States*, 517 U.S. 654, 660 (1996) (Court "granted certiorari to resolve disagreement among lower courts on the question whether Federal Rule 4, which authorizes an extendable 120-day period for service of process, supersedes the Suits in Admiralty Act provision that service on the United States

Besides, the very fact that nonparty shareholders will have to "adjust their conduct" to comply with the Seventh Circuit's new rule *favors* certiorari. Courts and commentators have long recognized the tendency of derivative litigation to lose its adversarial character and result in collusive deals between the company and plaintiffs' lawyers; for just as long, Rule 23.1 and the courts have encouraged unfettered shareholder participation as the key safeguard against such collusion. *See* Pet. at 14, nn.14 & 15. Requiring shareholders to "adjust their conduct" by filing motions to intervene imposes new costs and burdens (and thus decreases the likelihood) of their participation. *Id.* at 10, 14-17. Indeed, the Third Circuit expressly refused to require intervention motions for precisely these reasons. *Bell Atlantic*, 2 F.3d at 1310 (Rule 23.1's goal of preventing collusive settlements "cautions against creating obstacles to challenging derivative action settlement agreements"). *See also Gottlieb v. Wiles*, 11 F.3d 1004, 1010-11 (10th Cir. 1993);[8] Timothy A. Duffy, Note, *The Appealability of Class Action Settlements by Unnamed Parties*, 60 U. Chi. L. Rev. 933, 951 (1993) ("Duffy") (intervention inconsistent with "encourag[ing] fair settlements").

Even those shareholders who are not deterred by the additional burden associated with seeking intervention will, moreover, almost assuredly be denied leave to participate. Under Rule 23.1, shareholders are typically notified

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be made 'forthwith' "); *Carlisle v. United States*, 517 U.S. 416 (1996) (certiorari granted to determine whether trial court has authority under Fed. R. Crim. P. 29(c) to grant motion for acquittal even if it is untimely under that rule); *Celotex Corp. v. Edwards*, 511 U.S. 1105 (1994) (granting certiorari to resolve meaning of Fed. R. Civ. P. 65.1); *Pavelic & LeFlore v. Marvel Entertainment Group*, 493 U.S. 120, 122-23 (1989) (certiorari granted to resolve circuit split over interpretation of Fed. R. Civ. P. 11).

[8] Contrary to respondents' assertions, *Gottlieb* discussed *Bell Atlantic* approvingly and at length. *Id.*

of their right to participate only *after* the parties tentatively reach a settlement, and existing federal law strongly disfavors permitting intervention after a tentative settlement is reached. Pet. at 16 & n.18. Thus, no matter how shareholders may try to "adjust their conduct," the Seventh Circuit's rule will insulate flawed derivative settlements from any appellate scrutiny.[9] Finally, even if shareholders could somehow succeed in intervening, they would face all the duties associated with becoming a party, including duties to comply with automatic disclosure requirements, appear for depositions, answer interrogatories, and produce documents—plainly substantial deterrence to encouraging maximum shareholder participation. Pet. at 15-16.[10]

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[9] Respondents also cannot dispute that denials of motions to intervene are virtually unreviewable on appeal. Pet. at 13-14 & n.13. Indeed, some courts of appeals have even suggested that objecting shareholders' interests are always already adequately protected by party shareholders in Rule 23.1 proceedings. *See, e.g., id.; In re General Tire & Rubber Co. Sec. Litig.*, 726 F.2d 1075, 1087 (6th Cir.), *cert. denied*, 469 U.S. 858 (1984).

[10] Respondents argue that courts may permit shareholders to intervene "solely for the limited purpose of appeal." BIO at 14, n.9. But this assertion is wholly speculative: there is no federal rule shielding intervening parties from the ordinary duties of parties, and no certainty that the lower courts would manufacture such a rule. In fact, in their very next breath respondents argue *against* granting any such special protections. BIO at 14 (claiming it is "unfair to allow this individual shareholder to 'hold up' " the case without assuming "some responsibility").

The burdens associated with an intervention requirement are illustrated by the facts of this case. On May 30, 1997, the trial court tentatively approved the settlement. Only then were shareholders notified by mail of their right to participate (making it presumptively too late to intervene under federal law, *see* Pet. at 16, n.18). They were given just one month, until July 3, 1997, to review the parties' settlement, hire counsel, prepare and submit their objections, and appear before the court. The Seventh Circuit's rule would require shareholders also to prepare and argue a motion to intervene in this same limited amount of time.

3. Instead of defending the Seventh Circuit's express reliance on *Marino* and Federal Rule of Appellate Procedure 3(c) against petitioners' analysis, respondents suggest that the Seventh Circuit's decision is "sound" on an alternative ground. BIO at 12. Permitting individual shareholder appeals would, they argue, unduly " 'fragment' " and " 'confuse[]' " derivative suits. *Id.* But this argument, too, only underscores the depth of the disagreement between respondents and courts who believe it is imperative to avoid "creating obstacles" to shareholders' ability to participate in the appellate process as counterweight to the parties' natural tendency to collude. *Bell Atlantic*, 2 F.3d at 1310. *See also Gottlieb*, 11 F.3d at 1010-11; Duffy, 60 U. Chi. L. Rev. at 951. Besides, respondents lack any factual support for their empirical claim: courts, including the Seventh Circuit, have for decades permitted nonparty shareholder appeals without incident. And if allowing individual shareholder appeals *did* somehow create too much confusion, the appropriate remedy would not be to make parties out of individual shareholders but to preclude them from appeal altogether.

Respondents suggest that the Seventh Circuit's decision logically follows the fact that the nonparty shareholders have "no individual right to sue." BIO at 12-13. At best, however, this is another controversial view not shared by the Third Circuit (or apparently the Tenth Circuit and those commentators who approve of *Bell Atlantic*'s holding), and thus another reason favoring certiorari. Besides, while shareholders may not sue in their own names for damage done to the corporation, neither respondents nor the Seventh Circuit suggest that nonparty shareholders lack sufficient injury under Article III or 28 U.S.C. § 1291 to appeal a derivative settlement; to the contrary, the Seventh Circuit expressly recognizes that nonparty shareholders do have standing and criticizes the Third Circuit for conceiving of the issue simply as a standing question. Pet. App. at 7a.[11] Moreover, if any logical presumption follows, it is that a shareholder expressly allowed to object in the trial court under Rule 23.1 should be permitted to contest the disposition of its objections in the court of appeals. Indeed, the courts of appeals have routinely permitted appeals by an array of injured nonparties, and there is no reason to treat objecting shareholders any differently. Pet. at 20-21.[12]

[11] "Standing means injury in fact, and a reduction in the market price of one's stock is injury. Parties are a subset of injured persons. Equating injury with party status is exactly the approach disapproved by *Marino*." *Id.*

4. After "overrul[ing] *Tryforos*," the Seventh Circuit turned to consider whether, out of equity to petitioners, it should "defer the effect" of its ruling and apply its decision only prospectively. Pet. App. at 7a. The court, however, ultimately concluded that it was powerless to apply any new rule "concern[ing] jurisdiction" only prospectively, expressly acknowledging its "disagree[ment]" on this legal question with *George*. Pet. App. at 10a.

Respondents argue against granting certiorari on this second circuit split on the ground that no new rule was announced below. BIO at 15. But this argument (again) requires the Court to ignore the Seventh Circuit's own description of its holding both in this case and in *In re Brand Name*. *See* pp. 3-4, *supra*. Respondents fleetingly assert that, in any event, the Seventh Circuit's disagreement with the Ninth Circuit rises only to the level of "dictum." BIO at 15. But they never explain or defend this point. And here, too, they are at odds with the Seventh Circuit, which acknowledged that its disagreement

[12] Respondents discount petitioners' argument that leaving this split unresolved encourages forum shopping as "nonsensical and insulting to the federal judiciary." *Compare* Pet. at 17 *with* BIO at 11. In fact, however, the possibility of filing in a jurisdiction where any settlement is virtually guaranteed no appellate scrutiny would surely be an incentive to the plaintiffs' bar. And it is hardly insulting to the federal judiciary to suggest that improper settlements may evade judicial detection without the benefit of adversarial scrutiny that nonparty shareholder participation provides. Indeed, the Third Circuit has itself expressly worried about just this possibility. *Bell Atlantic*, 2 F.3d at 1310.

with the Ninth Circuit's decision in *George* is both genuine and pronounced. Pet. App. at 10a; *see also* Pet. at 24-25 (unrefuted explanation of split).

CONCLUSION

The petition for a writ of certiorari should be granted.

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JOINT APPENDIX

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PETITION FOR CERTIORARI FILED APRIL 21, 1998
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355 pp

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TABLE OF CONTENTS

	Page
Docket entries, United States District Court for the Northern District of Illinois	1
Docket entries, United States District Court for the Central District of Illinois	8
Docket entries, United States Court of Appeals for the Seventh Circuit	31
Complaint (July 13, 1995)	34
Memorandum Opinion and Order (Oct. 31, 1995)	43
Defendants' Motion to Dismiss (Dec. 27, 1995)	54
Consolidated and Amended Derivative Complaint (May 17, 1996)	56
Defendants' Motion to Dismiss (June 7, 1996)	93
Supplement to Consolidated and Amended Derivative Complaint (Nov. 4, 1996)	95
Amendment and Supplement to Consolidated and Amended Derivative Complaint (Dec. 6, 1996)	98
Agreed Motion for Order Preliminary Approving Settlement (May 30, 1997)	106
Stipulation of Settlement (May 29, 1997)	108
Exhibit A—Revisions to Board Procedures	128
Exhibit B-1—Notice of Hearing	134
Exhibit B-2—Summary Notice of Derivative Litigation Settlement	143
Order Preliminarily Approving Settlement (May 30, 1997)	146
Objections (Pauly) (June 13, 1997)	150
Objections (Berns) (June 23, 1997)	152
Objections (Chiara) (June 23, 1997)	154
Objections (Scott) (June 23, 1997)	155
Affidavit of Susan Salvetti (June 27, 1997)	157
Affidavit of Professor James L. Bicksler (June 27, 1997)	174
Motion for Final Approval (June 30, 1997)	193

TABLE OF CONTENTS—Continued

	Page
Joint Declaration of Terry Rose Saunders and Robert M. Roseman (June 30, 1997)	195
Affidavit of John C. Coffee, Jr. (June 25, 1997)	224
Declaration of R. Alan Miller (June 26, 1997)	245
Memorandum of ADM in Support of Settlement (July 1, 1997)	257
Affidavit of Michael P. Dooley (June 27, 1997)	276
Objections of California Public Employees' Retirement System *et al.* (July 2, 1997)	296
Declaration of Ann L. Yerger (July 2, 1997)	312
Declaration of Sarah A. B. Teslik (July 2, 1997	316
Declaration of John C. Coffee, Jr. (July 3, 1997)	326
Declaration of Robert M. Roseman (July 6, 1997)	328
Transcript of Fairness Hearing (July 7, 1997)	333
Notice of Appeal (July 14, 1997)	348
Plaintiffs' Motion To Dismiss Appeal of Non-Parties (Aug. 15, 1997)	350
Order Allowing Certiorari (September 29, 1998)	351

NOTICE

The following items have been omitted in printing this appendix because they appear on the following pages of the printed appendix to the petition for certiorari. They are incorporated herein by reference:

Final Judgment and Order of Dismissal of the District Court (July 7, 1997)	11a
Order of the District Court Awarding Attorneys' Fees and Reimbursement of Expenses (July 7, 1997)	16a
Opinion of the Court of Appeals	1a

Certificates of service whenever appended to documents appearing herein have been omitted in printing.

UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
(Chicago)

No. 95-CV-4006

PAUL FELZEN

v.

DWAYNE O. ANDREAS, *et al.*

DOCKET ENTRIES

Date	No.	PROCEEDINGS
7/11/95	1	COMPLAINT; jury demand—Civil cover sheet—Appearance(s) of Robert A. Wallner, Terry Rose Saunders, David J. Bershad and Peter D. Fishbein as attorney(s) for plaintiff with Rule 39 affidavit (no summons(es) issued.) (Documents: 1-1 through 1-4 (mk) [Entry date 07/12/95]
7/11/95	—	RECEIPT regarding payment of filing fee paid; on 7/11/95 in the amount of $120.00, receipt # 458174. (mk) [Entry date 07/12/95] [Edit date 07/12/95] [1:95cv4006]
7/12/95	—	RULE 39 letter mailed to Robert A. Wallner, David J. Bershad and Peter D. Fishbein (mk) [Edit date 07/12/95] [1:95cv4006]
7/26/95	2	VERIFICATION of Paul Flezen [*sic*] regarding complaint [1-1]; Notice of filing by plaintiff (ar) [Entry date 07/28/95] [1:95cv4006]

Date	No.	PROCEEDINGS
8/22/95	3	ATTORNEY APPEARANCE for defendant Archer Daniels Midland Co. by Aubrey M. Daniel III, Nancy F. Lesser, George A. Borden, Timothy Klenk, Richard J. Rappaport, Patricia Klein Smoots, Amy Manning (ar) (a) [Entry date 08/28/95] [1:95cv4006]
8/22/95	4	RULE 39 Affidavit of Aubrey M. Daniel III (ar) [Entry date 08/28/95] [1:95cv4006]
8/22/95	5	RULE 39 Affidavit of Nancy F. Lesser (ar) [Entry date 08/28/95] [1:95cv4006]
8/22/95	6	RULE 39 Affidavit of George A. Borden (ar) [Entry date 08/28/95] [1:95cv4006]
8/22/95	7	RULE 39 Affidavit of Timothy C. Klenk (ar) [Entry date 08/28/95] [1:95cv4006]
8/22/95	8	RULE 39 Affidavit of Richard J. Rappaport (ar) [Entry date 08/28/95] [1:95cv4006]
8/22/95	9	RULE 39 Affidavit of Patricia Klein Smoots (ar) [Entry date 08/28/95] [1:95cv4006]
8/22/95	10	RULE 39 Affidavit of Amy Beth Manning (ar) [Entry date 08/28/95] [1:95cv4006]
8/23/92	11	MOTION by plaintiff Paul Felzen for leave to withdraw appearance; Notice of motion (ar) [Entry date 08/28/95] [1:95cv4006]
8/23/95	12	MINUTE ORDER of 8/23/95 by Hon. Brian Barnett Duff: Denying plaintiff's motion for leave to withdraw appearance [11-1] for the reasons stated on the record. No notice (ar) [Entry date 8/28/95] [1:95cv4006]
8/31/95	13	RESPONSE by plaintiff Paul Felzen in opposition to defendants' motion for transfer; Notice of filing (ar) [Entry date 09/05/95] [1:95cv4006]

Date	No.	PROCEEDINGS
9/11/95	—	SCHEDULE set on 9/11/95 by Hon. Brian Barnett Duff: Status hearing set to 9:30 10/6/95. Mailed notice (ac) [1:95cv4006]
9/13/95	14	MOTION by defendant Archer Daniels Midland Company for an order entering the parties' stipulation extending time to move, answer or otherwise plead; Notice of motion (ar) [Entry date 09/15/95] [1:95cv4006]
9/13/95	15	STIPULATION extending time to move, answer or otherwise plead regarding defendant Archer Daniels Midlang [*sic*] Co.'s motion [14-1] (ar) [Entry date 09/15/95] [1:95cv 4006]
9/14/95	16	MINUTE ORDER of 9/14/95 by Hon. Brian Barnett Duff: Parties' agreed motion to extend time for defendants to answer the complaint [14-1] until 10 days after Judge Ruben Castillo rules on the pending motion for a finding that this action is related to the case of Lawrence v. Archer Daniels Midland Company, 95-C-3579, is granted. Mailed notice (ar) [Entry date 09/15/95] [Edit date 09/15/95] [1:95cv4006]
9/26/95	—	MOTION by Derivative plaintiff for extension of time in which to file proposed consolidated Derivative complaint; Notice of motion (Original in 95 C 3979) (eav) [Entry date 09/28/95] [1:95cv4006]
9/27/95	17	AMENDED MOTION by plaintiff Paul Felzen for leave to withdraw appearance (exhibit); Notice of motion (eav) [Entry date 09/28/95] [1:95cv4006]
9/27/95	18	MINUTE ORDER of 9/27/95 by Hon. Brian Barnett Duff: Status hearing reset for 10/26/95 at 9:30 a.m. Plaintiff's attorneys David J. Bershad and Robert A. Wallner mo-

Date	No.	PROCEEDINGS
		tion for leave to withdraw their appearances as counsel of record is granted. [17-1] Mailed notice (eav) [Entry date 09/28/95] [1:95cv 4006]
9/29/95	—	NOTICE by plaintiffs of proposed consolidated and amended derivative complaint (Exhibit) (Original in 95 C 3979) (Temporarily unavailable for docketing) (eav) [Entry date 10/05/95] [1:95cv4006]
10/4/95	19	MINUTE ORDER of 10/4/95 by Hon. Ruben Castillo: After reviewing the consolidated complaints that were filed in this case; Plaintiff's motion for finding of relatedness 14-1, Defendants' motion for reassignment of case 15-1, and defendants suppiemental motion for reassignment 24-1 are granted. The following cases are hereby reassigned to the calendar of Judge Castillo: 95 C 3980, 95 C 3985, 95 C 4006, 95 C 4028, 95 C 4031, 95 C 4032, 95 C 4036, 95 C 4037, 95 C 4041, 95 C 4091, 95 C 4093, 95 C 4223, 95 C 4234, 95 C 4535, and 95 C 5120. All defendants to answer the consolidated complaints by 10/16/95. Mailed notice (eav) [Entry date 10/05/95] [1:95cv4006]
10/6/95	20	REASSIGNMENT ORDER of 10/05/95: Case reassigned to Hon. Judge Ruben Castillo from Hon. Judge Brian Barnett Duff pursuant to local General Rule 2.31, Case consolidated 1:95-cv-3979 with member cases 1:35-cv-4006 (See reverse of minute order.) Mailed notice (eav) [Entry date 10/10/95] [1:95cv4006]
10/18/95	21	MINUTE ORDER of 10/18/95 by Hon. Ruben Castillo: Plaintiff's motion for extension of time in which the file proposed consolidated complaint [0-1] was previously granted by

Date	No.	PROCEEDINGS
		the court and should therefore be administratively terminated. No notice (eav) [Entry date 10/19/95] [1:95cv4006]
10/24/95	22	RESPONSE by defendant Archer Daniels to plaintiffs' supplemental memorandum; Notice of filing (eav) [Entry date 10/25/95] [1:95 cv4006]
10/24/95	23	MINUTE ORDER of 10/24/95 by Hon. Ruben Castillo: Unopposed motion of plaintiffs Felzen and Esner for leave to file additional appearances is granted. Jules Brody, Joseph H. Weiss and Robert D. Allison are granted leave to file their appearances on behalf of plaintiffs Paul Felzen and Sandra Esner. Mailed notice (eav) [Entry date 10/25/95] [1:95cv4006]
10/24/95	—	UNOPPOSED MOTION by plaintiffs Felzen and Esner for leave to file additional appearances; Notice of motion [Original in 95 C 3979) (eav) [Entry date 10/27/95] [1:95cv 4006]
10/25/95	—	MAILED Rule 3.14 letter to Robert D. Allison (eav) [1:95cv4006]
10/26/95	24	ATTORNEY APPEARANCE for plaintiff Paul Felzen by Jules Brody, Joseph H. Weiss, Robert D. Allison (eav) [Entry date 10/27/95] [1:95cv4006]
10/31/95	25	MEMORANDUM, OPINION, AND ORDER (eav) [Entry date 11/01/95] [1:95cv4006]
10/31/95	26	MINUTE ORDER of 10/31/95 by Hon. Ruben Castillo: Enter memorandum opinion and order. Defendants' motion to transfer this case to the Central District of Illinois is granted. These two cases are transferred to the Central District of Illinois in Danville., terminating case Mailed notice (eav) [Entry date 11/01/95] [1:95cv4006]

Date	No.	PROCEEDINGS
10/31/95	—	MOTION by defendants to dismiss the consolidated and amended derivative complaint or, in the alternative, to stay the action; Notice of filing. (Original in 95 C 3979) (mf) [Entry date 11/01/95] [1:95cv4006]
10/31/95	—	MEMORANDUM by defendants in support of defendants' motion to dismiss [0-1] or stay [0-2] (Attachment); Notice of filing. (Original in 95 C 3979) (mf) [Entry date 11/01/95] [1:95cv4006]
11/2/95	—	AGREED MOTION by defendants for leave to a joint memorandum in excess of 15 pages (Attachments); Notice of motion (Original in 95 C 3979) (eav) [Entry date 11/08/95] [1:95cv4006]
11/15/95	—	CERTIFIED AND TRANSMITTED the complete record to the USDC for the Springfield, Illinois (Danville) consisting of one volume of pleadings, transfer order and certified copy of docket entries, transmittal letter, and certificate, via certified mail no. P 863 997 749: Mailed copy of certificate and transmittal letter to counsel of record. (eav) [1:95cv 4006]
11/20/95	27	RETURN receipt no. P 863 997 749 from Springfield, Il. (eav) [Entry date 11/21/95] [1:95cv4006]
11/21/95	28	MINUTE ORDER of 11/21/95 by Hon. Ruben Castillo: Defendants' motion to dismiss [0-1], defendants' motion for leave to file a joint memorandum in excess of 15 pages [0-1] and defendants' motion to stay the action [0-2] are denied without prejudice. The parties are directed to refile these motions in the Central District of Illinois. No notice (eav) [Entry date 11/24/95] [1:95cv 4006]

Date	No.	PROCEEDINGS
12/1/95	—	MAILED on 12/01/95: Transmittal letter with original minute order of Judge Ruben Castillo, dated 11/21/95, document number 28 to Springfield, Illinois via certified mail no. P 863 997 752. Mailed copy of transmittal letter to counsel of record. (eav) [1:95cv 4006]
12/13/95	29	RETURN receipt no. P 863 997 752 (eav) [1:95cv4006]

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF ILLINOIS
(Urbana)

No. 95-CV-2279

PAUL FELZEN, *et al.*,
Plaintiffs,

v.

DWAYNE O. ANDREAS, *et al.*,
Defendants.

DOCKET ENTRIES

Date	No.	PROCEEDINGS
9/22/95	1	CONSOLIDATED CLASS ACTION COMPLAINT filed (no summons(es) issued) case referred to Mag. Judge David G. Bernthal (case was filed initially 07/10/95 in U.S. Dist Court, Northern District of IL, Chicago) (slj) [Entry date 11/22/95] [Edit date 02/26/96]
11/17/95	—	ORIGINAL FILE, (included doc's 1-26) certified copy of transfer order, (doc #26) and docket sheet received from Northern District of IL. Case referred to Mag. Judge David G. Bernthal (slj) [Entry date 11/22/95]
11/17/95	—	MINUTE-ENTRY: by Judge Harold A. Baker; pursuant to order entered 11/15/95 in the Northern District of IL, Chicago Division, this case has been transferred to the U. S. District Court for the Central District of IL, Urbana Division; previous case number in Northern District of IL 95-4006; new case number in the Urbana Division is 95-2279, all further pleadings are to be filed with the U.S. District Court, 201 S. Vine Street, Urbana, IL 61801 under the new case number 95-2279. (cc: all counsel) (slj) [Entry date 11/22/95]

Date	No.	PROCEEDINGS
12/27/95	2	MOTION by defendants to dismiss the consolidated and amended derivative complaint, or in the alternative to stay the action (slj) [Entry date 12/29/95]
12/27/95	3	MOTION by defendants for leave to file a joint memo in excess of 15 pages (slj) [Entry date 12/29/95]
12/27/95	4	CERTIFICATE OF INTEREST pursuant to Local Rule 1.6 filed by defendant Archer Daniels (slj) [Entry date 12/29/95]
1/3/96	—	ENDORSED ORDER on its face by Mag. Judge David G. Bernthal granting deft' motion for leave to file a joint memo in excess of 15 pages [3-1] (cc: all counsel). (slj)
1/3/96	—	MEMORANDUM IN SUPPORT of defts' motion to dismiss the consolidated and amended derivative complaint [2-1], of motion to stay the action [2-2] by defendants (slj)
1/5/96	9	CERTIFICATE OF INTEREST pursuant to Local Rule 1.6 filed by defendants (kc) [Entry date 01/10/95]
1/5/96	10	MOTION (filed in letter form) by defendant Archer Daniels to withdraw attorney Patricia Klein Smoots, Richard J Rappaport, Timothy C Klenk (kc) [Entry date 01/24/96]
1/10/96	6	MOTION by plaintiff Paul Felzen for leave to file response memo in excess of 15 pages (slj)

Date	No.	PROCEEDINGS
1/10/96	7	MOTION by plaintiff Paul Felzen to extend time to respond to defts' motion to dismiss (slj)
1/10/96	8	ATTORNEY APPEARANCE of Phebus and Glidden for plaintiff Paul Felzen (slj)
1/10/96	—	ENDORSED ORDER on its face by Judge Harold A. Baker granting motion to extend time to respond to defts' motion to dismiss [7-1], granting motion for leave to file response memo in excess of 15 pages [6-1] (cc: all counsel). (kc)
1/10/96	—	MINUTE-ENTRY: by Judge Harold A. Baker; Status hearing set 2:00 p.m. on 2/26/96 by personal appearance in Urbana, IL. Parties should be prepared to discuss alignment of the parties and cases and all pending matters. (cc: all counsel) (kc)
1/10/96	—	ENDORSED ORDER on its face by Judge Harold A. Baker granting motion to withdraw attorney Patricia Klein Smoots, Richard J Rappaport, Timothy C Klenk [10-1] attorney Patricia Klein Smoots for Archer Daniels, (cc: all counsel). (kc) [Entry date 01/24/96]
1/11/96	11	ATTORNEY APPEARANCE by Robert M Roseman, Jeffrey L Kodroff and Jacob A. Goldberg for plaintiff Paul Felzen (kc) [Entry date 01/24/96]
2/2/96	12	MEMORANDUM IN OPPOSITION motion to dismiss the consolidated and amended derivative complaint [2-1], motion to stay the action [2-2] by plaintiff Paul Felzen THIS DOCUMENT IS REPLACED BY NO. 16 FILED 2/26/96 (kc) [Edit date 02/26/96]

Date	No.	PROCEEDINGS
2/13/96	13	MOTION by plaintiff Paul Felzen for leave to file supplemental memo and exhibits in place of previously filed memo (#12) (kc) [Entry date 02/23/96]
2/16/96	14	CERTIFICATE OF INTEREST pursuant to Local Rule 1.6 filed by plaintiff Paul Felzen (kc) [Entry date 02/23/96]
2/16/96	15	ATTORNEY APPEARANCE of Jules Brody for plaintiff Paul Felzen (kc) [Entry date 02/23/96]
2/26/96	—	ENDORSED ORDER on its face by Judge Harold A. Baker granting motion for leave to file supplemental memo and exhibits in place of previously filed memo (#12) [13-1] (cc: all counsel). (kc)
2/26/96	16	MEMORANDUM IN OPPOSITION motion to dismiss the consolidated and amended derivative complaint [2-1], motion to stay the action [2-2] by plaintiff Paul Felzen REPLACES DOCUMENT NO. 12 FILED 2/2/96 (kc)
2/26/96	17	ATTORNEY APPEARANCE for defendant Howard G Buffett by George M. Garvey (kc) [Entry date 03/14/96]
2/26/96	18	MOTION by defendants for leave to file a reply brief in support of defendants' motion to dismiss or stay (kc) [Entry date 03/14/96]
2/26/96	—	MINUTE-ENTRY: by Judge Harold A. Baker; Status hearing held 2:00 2/26/96 Appearances: Terry Rose Saunders, Robert Allison, Joseph Phebus and Fred Isquith for pltfs; James Shafter, Aubrey Daniel for dft ADM; Thom Moss for individual defts; George Garvey for dft Buffett. Statement of the case by

Date	No.	PROCEEDINGS
		counsel. It is represented that this is a consolidated case that was transferred from the Northern District of Illinois (No. 95-4006 Felzen; 95-4041 Gaulich; and 95-4535 Esner). Prior to transfer 95-4041 (Gaulich) was dismissed without prejudice. The Clerk is directed to align the parties appropriately in accordance with counsel's representations. The parties agree that Joseph Phebus and Terry Rose Saunders are designated laison counsel for plaintiffs to receive all notices and distribute. James Shafter, Thom Moss and George Garvey are designated laison counsel for defts to receive and distribute notices. Motion for leave to file reply brief allowed. Reply brief on file. Parties represent the motion to dismiss or stay is fully briefed and the court sets for hearing the motion to dismiss the consolidated and amended derivative complaint or in the alternative to stay [2-1] at 1:30 4/26/96 by personal appearance in Urbana, IL. See Case Management Order # 1. (cc: designated counsel) (kc) [Entry date 03/14/96]
2/26/96	—	ENDORSED ORDER on its face by Judge Harold A. Baker granting motion for leave to file a reply brief in support of defendants' motion to dismiss or stay [18-1] (cc: designated counsel). (kc) [Entry date 03/14/96]
2/26/96	19	REPLY by defendants to response to motion to dismiss the consolidated and amended derivative complaint [2-1], motion to stay the action [2-2] (kc) [Entry date 03/14/96]
3/6/96	20	CASE MANAGEMENT ORDER NO. 1 by Judge Harold A. Baker (cc: designated counsel) (kc) [Entry date 03/14/96]

Date	No.	PROCEEDINGS
3/29/96	21	MOTION by defendants for protective order (kc) [Entry date 04/22/96]
3/29/96	22	MOTION by defendants for oral argument on defendants' motion for a protective order and for advancement of oral argument on defendants' motion to dismiss (kc) [Entry date 04/22/96]
3/29/96	23	MEMORANDUM IN SUPPORT of motion for oral argument on defendants' motion for a protective order and for advancement of oral argument on defendants' motion to dismiss [22-1] by defendants (kc) [Entry date 04/22/96]
4/11/96	24	MOTION by plaintiff for leave to file surreply in opposition to defendants' motion to dismiss or stay (kc) [Entry date 04/22/96]
4/15/96	25	RESPONSE by plaintiffs to motion for oral argument on defendants' motion for a protective order and for advancement of oral argument on defendants' motion to dismiss [22-1] (kc) [Entry date 04/2/96]
4/15/96	26	MEMORANDUM IN OPPOSITION motion for oral argument on defendants' motion for a protective order and for advancement of oral argument on defendants' motion to dismiss [22-1] by plaintiffs (kc) [Entry date 04/22/96]
4/22/96	—	ENDORSED ORDER on its face by Judge Harold A. Baker allowing motion for leave to file surreply in opposition to defendants' motion to dismiss or stay (kc)
4/22/96	27	SURREPLY by plaintiffs to opposition to motion to dismiss the consolidated and amended derivative complaint [2-1], motion to stay the action [2-2] (kc)

Date	No.	PROCEEDINGS
4/26/96	—	MINUTE-ENTRY: by Judge Harold A. Baker Appearances: Terry Rose Saunders and Robert Roseman for pltfs; James Shafter, Aubrey Daniel, Nancy Lessr and George Borden for dft ADM; Thom Moss for individual dfts and George Garvey for dft Buffett Arguments heard on motion to dismiss. Court grants motion to dismiss the consolidated and amended derivative complaint (which the court does not have in the official court file) [2-1], pltf given 21 days to replead. Dfts to resp within 21 days thereafter. (cc: Phebus, Saunders, Shafter, Moss & Garvey) (kc) [Entry date 05/29/96]
5/17/96	28	AMENDED COMPLAINT by plaintiff Paul Felzen, plaintiff Sandra Esner; jury demand; adding Ray A Goldberg, John K Vanier, Shreve M Archer Jr, F Ross Johnson, M Brian Mulroney, Robert S. Strauss, and Margaretta Rockefeller (kc) [Entry date 05/29/96]
6/7/96	29	MOTION by defendant to dismiss the consolidated and amended derivative complaint for failure to make demand and failure to state a claim (kc) [Entry date 06/12/96]
6/7/96	30	MOTION by defendants for leave to file joint memorandum in excess of fifteen pages (kc) [Entry date 06/12/96]
6/12/96	—	ENDORSED ORDER on its face by Judge Harold A. Baker granting motion for leave to file joint memorandum in excess of fifteen pages [30-1] (cc: all counsel). (kc)
6/12/96	31	MEMORANDUM IN SUPPORT of motion to dismiss the consolidated and amended derivative complaint for failure to make demand and failure to state a claim [29-1] by defendants (kc)

Date	No.	PROCEEDINGS
6/18/96	32	MOTION by plaintiffs for leave to file brief in excess of 15 pages, and to extend time to file the same (slj) [Entry date 07/08/96]
7/9/96	—	ENDORSED ORDER on its face by Mag. Judge David G. Bernthal granting motion for leave to file brief in excess of 15 pages [32-1], granting motion to extend time to file the same [32-2] (cc: all counsel). (slj)
7/10/96	33	MOTION by plaintiffs to compel discovery (slj)
7/10/96	34	MEMORANDUM IN SUPPORT of motion to compel discovery [33-1] by plaintiffs (slj)
7/10/96	35	MEMORANDUM IN OPPOSITION motion to dismiss the consolidated and amended derivative complaint for failure to make demand and failure to state a claim [29-1] by plaintiffs (slj)
7/10/96	36	CERTIFICATE of service re doc's #33-35 by plaintiffs (slj)
7/19/96	37	MEMORANDUM IN OPPOSITION motion to compel discovery [33-1] by defendant Archer Daniels (mt)
8/13/96	38	MOTION by defendants, for leave to file reply brief in support of defendants' motion to dismiss (kc) [Entry date 09/04/96]
9/4/96	—	ENDORSED ORDER on its face by Judge Harold A. Baker granting motion for leave to file reply brief in support of defendants' motion to dismiss [38-1] (cc: all counsel). (kc)
9/4/96	39	REPLY by defendant, plaintiff, defendant to response to motion to dismiss the consolidated and amended derivative complaint for failure to make demand and failure to state a claim [29-1] (kc)

Date	No.	PROCEEDINGS
9/4/96	—	MINUTE-ENTRY: by Judge Harold A. Baker setting motion to compel discovery [33-1] at 1:30 9/26/96, setting motion to dismiss the consolidated and amended derivative complaint for failure to make demand and failure to state a claim [29-1] at 1:30 9/26/96. The Court finds the defendants' motion for a protective order and for advancement of oral argument on defendants' motion to dismiss [22-1] moot due to the filing of the amended complaint. (cc: designated counsel) (kc)
9/24/96	40	JOINT MOTION by plaintiffs and defendants to continue hearing set 9/26/96 (mt)
9/25/96	—	MINUTE-ENTRY: by Judge Harold A. Baker granting motion to continue hearing set 9/26/96 [40-1], re motion to compel discovery [33-1], re motion to dismiss the consolidated and amended derivative complaint for failure to make demand and failure to state a claim [29-1]. Hearing set 9/26/96 is VACATED and will be reset. Atty Peckert is directed to notify all parties. (mt)
10/10/96	—	MINUTE-ENTRY: by Judge Harold A. Baker setting motion to compel discovery [33-1] at 1:30 11/8/96, setting motion to dismiss the consolidated and amended derivative complaint for failure to make demand and failure to state a claim [29-1] at 1:30 11/8/96 by personal appearance in Urbana. (cc: attys Joseph Phebus, Terry Rose Saunders, James Shafter, Thom Moss, George Garvey) (mt)
10/22/96	41	MOTION by plaintiff Paul Felzen for leave to file reply in support of motion to compel discovery (mt)
10/24/96	—	ENDORSED ORDER on its face by Judge Harold A. Baker granting motion for leave to

Date	No.	PROCEEDINGS
		file reply in support of motion to compel discovery [41-1] (cc: all counsel). (mt)
10/24/96	42	REPLY by plaintiff Paul Felzen, plaintiff Sandra Esner to response to motion to compel discovery [33-1] (mt)
10/31/96	—	MINUTE-ENTRY: by Judge Harold A. Baker VACATING motion hearing 11/8/96 and RESETTING motion to compel discovery [33-1] at 1:30 12/11/96, RESETTING motion to dismiss the consolidated and amended derivative complaint for failure to make demand and failure to state a claim [29-1] at 1:30 12/11/96 by personal appearance in Urbana. (cc: attys Phebus, Saunders, Shafter, Moss & Garvey (slj) [Edit date 10/31/96]
11/4/96	43	MOTION by plaintiff Paul Felzen, plaintiff Sandra Esner for leave to file supplement to consolidated and amended derivative complaint (sj) [Entry date 11/06/96]
11/4/96	44	MEMORANDUM IN SUPPORT of motion for leave to file supplement to consolidated and amended derivative complaint [43-1] by plaintiff Paul Felzen, plaintiff Sandra Esner (sj) [Entry date 11/06/96]
11/18/96	—	ENDORSED ORDER on its face by Judge Harold A. Baker granting pltfs' motion for leave to file supplement to consolidated and amended derivative complaint [43-1] (cc: all counsel). (sj)
11/18/96	45	MOTION by dfts Dwayne O Andreas, Ralph Bruce, John H Daniels, Howard G Buffett, Lowell W Andreas, James R Randall, Michael D Andreas, H D Hale, O Glenn Webb, Martin L Andreas, Archer Daniels, Ray A Goldberg, John K Vanier, Shreve M Archer Jr, F Ross

Date	No.	PROCEEDINGS
		Johnson, M Brian Mulroney, Robert S Strauss, Margaretta Rockefeller for protective order (sj) [Entry date 11/19/96]
11/18/96	46	MEMORANDUM IN SUPPORT of motion for protective order [45-1] by dfts Dwayne O Andreas, Ralph Bruce, John H Daniels, Howard G Buffett, Lowell W Andreas, James R Randall, Michael D Andreas, H D Hale, O Glenn Webb, Martin L Andreas, Archer Daniels, Ray A Goldberg, John K Vanier, Shreve M Archer Jr, F Ross Johnson, M Brian Mulroney, Robert S Strauss, Margaretta Rockefeller (sj) [Entry date 11/19/96]
11/18/96	47	CERTIFICATE of service re mtn for protective order (#45) and supporting memo (#46) by defendants (sj) [Entry date 11/19/96]
11/18/96	43	AMENDMENT (SUPPLEMENT) by plaintiff Paul Felzen, plaintiff Sandra Esner to consolidated and amended derivative complaint [28-1] (attached as Exhibit A to mtn #43) (sj) [Entry date 01/02/97]
12/2/96	48	RESPONSE by plaintiff Paul Felzen, plaintiff Sandra Esner to motion for protective order [45-1 (sj) [Entry date 12/03/96]
12/6/96	49	MOTION by plaintiff Paul Felzen for leave to amend and supplement their consolidated & amended derivative complaint (slj)
12/6/96	50	MEMORANDUM IN SUPPORT of motion for leave to amend and supplement their consolidated & amended derivative complaint [49-1] by plaintiff Paul Felzen (slj)
12/10/96	—	MINUTE-ENTRY: conf call held by Judge Harold A. Baker with appearance of attys Roseman, Shafter, Daniel and Borden. Oral

Date	No.	PROCEEDINGS
		mtn to continue hrg set for 12/11/96 made by all parties; mtn allowed. Motion to dismiss the consolidated and amended derivative complaint for failure to make demand and failure to state a claim [29-1] and motion to compel discovery [33-1] RESET to 1:30 1/21/97 by personal appearance in Urbana, IL. (sj) [Entry date 12/11/96]
12/23/96	—	MINUTE-ENTRY: by Judge Harold A. Baker. Motion hearing set 1/21/97 is VACATED AND RESET at 1:30 1/21/97 by personal appearance in Urbana re motion for leave to amend and supplement their consolidated & amended derivative complaint [49-1]; motion for protective order [45-1]; motion to compel discovery [33-1]; motion to dismiss the consolidated and amended derivative complaint for failure to make demand and failure to state a claim [29-1]. (cc: all counsel) (mt)
12/27/96	—	ENDORSED ORDER on its face by Judge Harold A. Baker granting motion for leave to amend and supplement their consolidated & amended derivative complaint [49-1] (cc: all counsel). (mt)
12/27/96	49	AMENDMENT AND SUPPLEMENT by plaintiff Paul Felzen, plaintiff Sandra Esner to consolidated and amended derivative complaint [28-1], [43-1] (attached as Exhibit A to document #49) (sj) [Entry date 01/02/97]
1/23/97	—	MINUTE-ENTRY: by Judge Harold A. Baker; By agreement of parties the motion hearing 1/31/97 is VACATED AND RESET AT 1:30 2/26/97. Resetting motion for protective order [45-1]; motion to compel discovery [33-1] and motion to dismiss the consolidated and amended derivative complaint

Date	No.	PROCEEDINGS
		for failure to make demand and failure to state a claim [29-1] at 1:30 2/26/97 (cc: all counsel) (slj)
2/5/97	51	MOTION by defendant Archer Daniels for leave to file to file joint supplemental memorandum in support of the pending motion to dismiss pla's derivative complaint (kw)
2/5/97	52	CERTIFICATE of service by defendant Archer Daniels (kw)
2/7/97	—	ENDOSED ORDER on its face by Judge Harold A. Baker granting dfts' motion for leave to file to file [*sic*] joint supplemental memorandum in support of the pending motion to dismiss pla's derivative complaint [51-1] (cc: Joseph Phebus, Terry Rose Saunders, James Shafter, Thom Moss and George Garvey as agreed per docket entry dated 2/26/96) (sj) [Edit date 02/07/97]
2/7/97	53	SUPPLEMENTAL MEMORANDUM IN SUPPORT of motion to dismiss the consolidated and amended derivative complaint for failure to make demand and failure to state a claim [29-1] by defendants (sj)
2/14/97	—	MINUTE-ENTRY: by Judge Harold A. Baker; by agreement of parties, motion hearing set 2/26/97 is vacated; RESETTING motion for protective order [45-1], motion to compel discovery [33-1], and motion to dismiss the consolidated and amended derivative complaint for failure to make demand and failure to state a claim [29-1] at 1:30 3/26/97 by personal appearance in Urbana. Parties to advise the court at the earliest opportunity whether the 3/26/97 hearing will be a status hearing or a motion hearing; if it will be a motion hearing, the date may need to be re-

Date	No.	PROCEEDINGS
		scheduled to allow adequate time. (cc: designated counsel) (sj)
2/18/97	54	MOTION by plaintiff Paul Felzen, plaintiff Sandra Esner to extend time to file response to dfts' supplemental memo in support of mtn to dismiss pltfs' derivative complaint (sj) [Entry date 02/20/97]
3/4/97	—	ENDORSED ORDER on its face by Judge Harold A. Baker; response to dfts' supplemental memorandum is support of mtn to dismiss pltfs' derivative cmp [53-1] is due by 3/7/97. (cc: designated counsel) (sj) [Edit date 03/04/97]
3/6/97	55	AGREED MOTION by plaintiffs and defendants to extend time for pltfs to respond to dfts' supplemental memo in support of pending mtn to dismiss pltfs' derivative complaint until 3/26/97 (sj)
3/6/97	56	ORDER by Mag. Judge David G. Bernthal granting agreed motion to extend time for pltfs to respond to dfts' supplemental memo in support of pending mtn to dismiss pltfs' derivative complaint until 3/26/97 [55-1] ; response to memorandum [53-1] due 3/26/97. (cc: designated counsel) (sj)
3/26/97	—	MINUTE-ENTRY: by Judge Harold A. Baker VACATING mtn hrg set for 3/26/97 and RESETTING motion for protective order [45-1] at 2:30 4/4/97, motion to compel discovery [33-1] at 2:30 4/4/97, motion to dismiss the consolidated and amended derivative complaint for failure to make demand and failure to state a claim [29-1] at 2:30 4/4/97 by personal appearance in Urbana. Atty Peckert to give notice. (sj)

Date	No.	PROCEEDINGS
3/26/97	57	AGREED MOTION by plaintiffs and defendants to extend time for the filing of pltfs' response to dfts' supplemental memo in support of pending mtn to dismiss pltfs' derivative complaint (sj)
3/27/97	58	ORDER by Judge Harold A. Baker granting motion to extend time for the filing of pltfs' response to dfts' supplemental memo in support of pending mtn to dismiss pltfs' derivative complaint [57-1]; response ddl to memorandum [53-1] extended to 4/4/97 (cc: designated counsel) (sj) [Edit date 03/27/97]
3/27/97	59	Notice of hearing filed by dft ADM; status hearing set 2:30 4/4/97 before Judge Harold A. Baker in Urbana, IL. (sj)
4/4/97	—	MINUTE-ENTRY: by Judge Harold A. Baker; Rule 16 hearing held in chambers 2:30 4/4/97—app of pltfs by Robert Roseman and Terry Rose Saunders, app of individual dfts by Thom Moss, app of dft ADM by James Shafter. Status of case discussed; Rule 16 conference set 1:30 4/25/97 by conf call. Hearing set 7/7/97 on all pending matters; setting motion for protective order [45-1] at 9:00 7/7/97, setting motion to compel discovery [33-1] at 9:00 7/7/97, setting motion to dismiss the consolidated and amended derivative complaint for failure to make demand and failure to state a claim [29-1] at 9:00 7/7/97 by personal appearance in Urbana, IL. All matters stayed until the 7/7/97 hearing. (sj) [Entry date 04/07/97]
4/25/97	—	MINUTE-ENTRY: by Judge Harold A. Baker; Rule 16 conference held 1:30 4/25/97. Apr of pltf thru Terry Rose Saunders, apr of individual defts thru Thom Moss and apr of ADM thru James Shafter. Status discussed. No further hrgs set. (slj)

Date	No.	PROCEEDINGS
5/28/97	—	MINUTE-ENTRY: by Judge Harold A. Baker; at request of atty Shafter, conference call held with attorneys Terry Rose Saunders and James Shafter. Parties working on a proposed notice that they propose to mail out on 5/30/97 if they can get the court's approval. Telephone conference call set 10:30 5/30/97; atty Shafter to set up the call and notify parties and the court what telephone number to call into.
5/30/97	60	AGREED MOTION by plaintiff Paul Felzen, plaintiff Sandra Esner for order preliminarily approving settlement, scheduling a final settlement hearing and directing that notice be given to the shareholders of ADM Co. (sj) [Entry date 06/03/97]
5/30/97	61	MEMORANDUM IN SUPPORT of agreed motion for order preliminarily approving settlement, scheduling a final settlement hearing and directing that notice be given to the shareholders of ADM Co. [60-1] by plaintiff Paul Felzen, plaintiff Sandra Esner (sj) [Entry date 06/03/97]
5/30/97	—	MINUTE-ENTRY: by Judge Harold A. Baker; status hearing held by conf call 10:30 5/30/97—app of pltfs by Terry Rose Saunders; app of dfts by James Shafter, George Borden, James Peckert, Thom Moss; app of Delaware pltfs by Susan Salvetti, Mel Lifshitz, Jeffrey Haber. Statement by the court as to order; written order to be entered this date. (sj) [Entry date 06/03/97]
5/30/97	62	ORDER by Judge Harold A. Baker granting agreed motion for order preliminarily approving settlement, scheduling a final settlement hearing and directing that notice be given to the shareholders of ADM Co. [60-1];

Date	No.	PROCEEDINGS
		settlement hearing set 9:30 7/7/97 at the U.S. Courthouse in Urbana, IL to determine whether the proposed settlement of the derivative claims on the terms and conditions provided in the Stipulation is fair, reasonable and adequate and should be approved by the court; whether a judgment, as provided in the stipulation should be entered herein and to determine whether pltfs' counsels' fees and expenses should be approved. See written order, (cc: designated counsel; copy faxed to attys Haber, Saunders, Shafter and Moss) (sj) [Entry date 06/04/97]
6/13/97	63	OBJECTIONS by objector Charles W Pauly Jr, objector Elizabeth Pauly to proposed settlement of derivative actions (sj) [Entry date 06/16/97]
6/23/97	65	OBJECTIONS by objector Peter D Scott to motion for order preliminarily approving settlement, scheduling a final settlement hearing and directing that notice be given to the shareholders of ADM Co. [60-1] (slj) [Entry date 06/30/97]
6/26/97	64	OBJECTIONS by objector Mitchell Berns to award of excessive attorneys' fees (kw) [Entry date 06/27/97]
6/26/97	66	OBJECTIONS by objector John P Chiara to motion for order preliminarily approving settlement, scheduling a final settlement hearing and directing that notice be given to the shareholders of ADM Co. [60-1] (slj) [Entry date 06/30/97]
6/30/97	67	AFFIDAVIT of Susan Salvetti in support of the proposed settlement and the petition of Delaware Pltfs' Counsel for Attys' fees and reimbursement of expenses. [60-1] (slj)

Date	No.	PROCEEDINGS
6/30/97	68	MEMORANDUM IN SUPPORT of of proosed [*sic*] settlement and award of fees and expenses [60-1] by miscellaneous Delaware Plaintiffs (slj)
6/30/97	69	APPENDIX filed by miscellaneous Delaware Plaintiffs re affidavit [67-1] (slj)
6/30/97	70	NOTICE of filing and service re doc's 68 & 69 by miscellaneous Delaware Plaintiffs (slj)
6/30/97	71	MOTION by plaintiffs for final approval of the proposed settlement and pltfs' counsel's joint application for an award of attys' fees and reimbursement of expenses (slj)
6/30/97	72	AFFIDAVIT of Terry Rose Saunders and Robert M. Roseman in support of the proposed settlement and pltfs' counsel's joint application for an award of attys' fees and reimbursement of expenses [71-1] (slj)
6/30/97	73	MEMORANDUM IN SUPPORT of joint application for an award of attys' fees and reimbursement of expenses [71-1] (slj)
6/30/97	74	APPENDIX filed by plaintiff in support of the proposed settlement and pltfs' counsel's joint application for an award of attys' fees and reimbursement of expenses [71-1] (slj)
6/30/97	75	MEMORANDUM IN SUPPORT of the proposed settlement by plaintiff Paul Felzen, plaintiff Sandra Esner (slj)
6/30/97	76	CERTIFICATE of service re doc's 71-75 by plaintiffs (slj)
7/1/97	77	MOTION by defendant Archer Daniels for leave to file memo exceeding page limitation (mb)
7/2/97	—	ENDORSED ORDER on its face by Judge Harold A. Baker granting motion for leave

Date	No.	PROCEEDINGS
		to file memo exceeding page limitation [77-1] (cc: all counsel). (slj)
7/2/97	78	MEMORANDUM IN SUPPORT of settlement by defendant Archer Daniels (slj)
7/2/97	79	AFFIDAVIT of Michael P. Dooley in support of Settlement with attached exhibits (slj)
7/3/97	80	OBJECTIONS by objector CA Public Employees, objector FL State Board to proposed settlement of derivative actions (slj)
7/3/97	81	DECLARATION of Ann L. Yerger re proposed settlement (slj)
7/3/97	82	DECLARATION of Steven F. Benz (slj)
7/3/97	83	DECLARATION of Sarah A.B. Teslik re proposed settlement (slj)
7/7/97	84	SUPPLEMENT by objector Mitchell Berns to objection of Mitchell Berns to award of excessive attys' fees [64-1] (slj)
7/7/97	85	ATTORNEY APPEARANCE by Michael Dockterman for defendant O Glenn Webb (mt) [Entry date 07/08/97]
7/7/97	86	AFFIDAVIT of Christine Ferguson regarding mailing of notice of hearing on proposed settlement of derivative actions and errata (mt) [Entry date 07/08/97]
7/7/97	87	AFFIDAVIT of John C. Coffee, Jr. to supplement earlier affidavit dated 6/25/97 (mt) [Entry date 07/08/97]
7/7/97	88	AFFIDAVIT of Robert M. Roseman in opposition to objectors' motion to postpone the settlement hearing (mt) [Entry date 07/08/97]
7/7/97	89	SUPPLEMENTAL AFFIDAVIT of C. Oliver Burt, III (mt) [Entry date 07/08/97]

Date	No.	PROCEEDINGS
7/7/97	—	MINUTE-ENTRY: by Judge Harold A. Baker re motion for final approval of the proposed settlement and pltfs' counsel's joint application for an award of attys' fees and reimbursement of expenses [71-1], re motion for protective order [45-1], re motion to compel discovery [33-1], re motion to dismiss the consolidated and amended derivative complaint for failure to make demand and failure to state a claim [29-1]. Mtn hrg held 7/7/97. Appearances as follows: Joseph Phebus/Robert Roseman/Terry Rose Saunders for Illinois pltfs; Stanley Bernstein/Susan Salvetti/Robert Harwood for Delaware pltfs; Thom Moss for individual dfts; Michael Dockterman for individual dft Webb; James Peckert/A. James Shafter for dft ADM; objectors: Mark Hansen for objectors California Public Employees' Retirement System and Florida State Board of Administration; Tom Beenck for Florida State Board Administration; objector Miller; Martin Glotzer (non-atty) representing 25% of shareholders. Mtn by objectors to postpone hearing on settlement; arguments hrd; crt concludes due process was afforded; mtn denied. Arguments heard on settlement; court concludes settlement is fair and reasonable and adequate. Crt waives page limitation on filing by Florida State Board (#88). Arguments heard on atty fees. Crt concludes gross fees 49% of settlement fund: $3,920,000 awarded including expenses. 60% to Illinois pltfs attys $2,253,000; 40% to Delaware pltfs attys $1,568,000. Final judgment order of dismissal entered. Order awarding fees entered. See written orders. (mt) [Entry date 07/08/97]

Date	No.	PROCEEDINGS
7/7/97	90	ORDER by Judge Harold A. Baker granting motion for final approval of the proposed settlement and pltfs' counsel's joint application for an award of attys' fees and reimbursement of expenses [71-1]. The court hereby approves the settlement set forth in the stipulation and finds the settlement is, in all respects, fair, reasonable and adequate; the crt hereby dismisses this action against the company w/prej and w/out costs; the crt retains jurisdiction over the settlement. See written order. Case terminated. (cc: all counsel) (mt) [Entry date 07/08/97]
7/7/97	91	ORDER AWARDING ATTORNEYS' FEES AND REIMBURSEMENT OF EXPENSES by Judge Harold A. Baker. The crt awards gross fees and expenses to pltfs attys in amt of 49 percent of the settlement proceeds ($3,920,000). These fees and expenses shall be divided 60 percent to the federal action or $2,352,000 and 40 percent or $1,568,000 to the Delaware actions. See written order. (cc: all counsel) (mt) [Entry date 07/08/97]
7/7/97	92	EXHIBIT No. 1 for fairness hrg (letter by Kehart, Shafter & Webber) for plaintiff Paul Felzen stored in file 95-2279 (mt) [Entry date 07/08/97]
7/8/97	93	JUDGMENT in a civil case entered. Case dismissed w/ prej as compromised. (cc: all counsel) (mt)
7/15/97	94	NOTICE of APPEAL by objector CA Publi. Employees, objector FL State Board from Dist. Court decision, [90], [91], [93] (cc: designated counsel and counsel for objectors and misc parties) (sj) [Entry date 07/16/97] [Edit date 07/16/97]

Date	No.	PROCEEDINGS
7/15/97	95	JURISDICTIONAL DOCKETING STATEMENT filed by objector CA Public Employees, objector FL State Board (sj) [Entry date 07/16/97]
7/15/97	96	Received appeal fee in amount of $105.00 (Receipt # 032269) (sj) [Entry date 07/16/97]
7/16/97	97	SHORT RECORD ON APPEAL sent to USCA (sj)
7/21/97	98	DESIGNATION OF RECORD by objector CA Public Employees, objector FL State Board (sj)
7/21/97	99	Request by objector CA Public Employees, objector FL State Board for transcript (pink copy of SEVENTH CIRCUIT TRANSCRIPT INFORMATION SHEET) (sj)
7/23/97	100	RESPONSE (filed as REPLY) by objector Charles W Pauly Jr, objector Elizabeth Pauly to motion for final approval of the proposed settlement and pltfs' counsel's joint application for an award of attys' fees and reimbursement of expenses [71-1] (sj)
7/28/97	101	Notification by USCA of Appellate Docket Number 97-2829 (sj)
7/29/97	102	MOTION by objector CA Public Employees, objector FL State Board to withdraw the record on appeal (sj)
8/1/97	103	TRANSCRIPT of Fairness Hearing held 7/7/97 before Judge Harold A. Baker filed by Toni Judd, U.S. Court Reporter (sj)
8/5/97	104	ORDER by Mag. Judge David G. Bernthal granting motion to withdraw the record [102-1] (cc: all counsel) (slj)

Date	No.	PROCEEDINGS
8/5/97	105	Remark-Appeal record consisting of 2 volumes of pleadings, 1 transcript and 6 loose pleadings mailed to LAW FIRM OF KELLOGG HUBER, Washnigton, DC. (slj)
8/21/97	106	COPY of USCA Order directing Appellant California Public Employees Retirement System and Florida State Board of Administration to file a response to pltfs' motion to dismiss the appeal of non-parties, filed on 8/14/97. (slj)
9/4/97	107	Remark—appeal record consisting of 2 volumes of pleadings, 1 transcript and 6 loose pleadings returned from law firm of KELLOGG HUBER HANSEN TODD & EVANS in Washington, DC (sj)
2/17/98	108	MANDATE from USCA dismissing the appeal [94-1] for want of jurisdiction, with costs, in acocrdance with the decision of that court entered by that court on 1/21/98 (sj)

UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

No. 97-2829

PAUL FELZEN,
Trustee of Louise Laskin Trust—1991,
and SANDRA ESNER,
Plaintiffs-Appellees,

v.

ARCHER DANIELS MIDLAND COMPANY,
a Delaware Corporation,
Defendant.

Appeal of: California Public Employees
Retirement System and Florida
State Board of Administration

DOCKET ENTRIES

Date	PROCEEDINGS
7/21/97	Private civil case docketed. [97-2829] [969479-1] Transcript information sheet due 7/31/97. Appellant's brief due 9/2/97 for CA Public Employees, for FL State Bd of Admin. (dorh)
7/21/97	Filed Appellant CA Public Employees, Appellant FL State Bd of Admin docketing statement. [97-2829] [969516-1] (dorh)
7/31/97	Certificate of interest filed by Appellant CA Public Employees, Appellant FL State Bd of Admin. [97-2829] [969479-1] (jenp)

Date	PROCEEDINGS
8/1/97	Certificate of interest filed by Appellee Paul Felzen, Appellee Sandra Esner. [97-2829] [969479-1] (jenp)
8/8/97	Certificate of interest filed by Archer-Daniels-Midla [*sic*]. [97-2829] [969479-1] (jenp)
8/8/97	Added attorney A. James Shafter per appearance form. Appearance form filed for Archer-Daniels-Midla [*sic*] by attorney A. James Shafter, James E. Peckert. [97-2829] [969479-1] (jenp)
8/13/97	Certificate of interest filed by defendants-appellees, Dwayne and Michael Adreas, et al., (Notice-Only). [97-2829] [969479-1] (jenp)
8/15/97	Filed motion by Appellees Paul Felzen and Sandra Esner to dismiss appeal of non-parties. [978129-1] [97-2829] (heid)
8/18/97	ORDER: Filed clerk's notice to Appellant CA Public Employees, Appellant FL State Bd of Admin to file a response to PLAINTIFFS' MOTION TO DISMISS THE APPEAL OF NON-PARTIES. [978129-1] MAF [97-2829] [978412-1] Briefing is SUSPENDED pending resolution of the motion. (See order for further details) Response due 8/29/97 for FL State Bd of Admin, for CA Public Employees. (patb)
8/29/97	Filed Appellants CA Public Employees and FL State Bd of Admin Memorandum In Opposition to plaintiffs' motion to dismiss case. [982755-1] [97-2829] [982755-1] (heid)
9/4/97	ORDER: Filed clerk's notice to Plaintiffs Paul Felzen and Sandra Esner to file a response to MEMORANDUM IN OPPOSITION TO PLAINTIFFS' MOTION TO DISMISS. [978129-1] MAF [97-2829] Response due 9/17/97 for Sandra Esner, for Paul Felzen. Briefing remains DEFERRED pending resolution of the motion to dismiss. (heid)

Date	PROCEEDINGS
9/17/97	Filed Appellees Paul Felzen and Sandra Esner Reply Memorandum In Support of motion to dismiss case. [989012-1] [97-2829] [989012-1] (heid)
1/21/98	Filed opinion of the court by Judge Easterbrook. This appeal is DISMISSED for want of jurisdiction. (This opinion was circulated before release to all judges in active service. See Circuit Rule 40(e). No judge favored hearing the case en banc.) Chief Judge Richard A. Posner, Circuit Judge Joel M. Flaum, Circuit Judge Frank H. Easterbrook. [97-2829] [969479-1] (patb)
1/21/98	ORDER: Final judgment filed per opinion. With costs: y. [97-2829] [1025507-1] (patb)
2/12/98	MANDATE ISSUED. No record to be returned. [97-2829] [969479-1] (nick)
2/20/98	Filed mandate receipt. [97-2829] [1034510-1] (fran)
4/27/98	Filed notice from the Supreme Court of the filing of a Petition for Writ of Certiorari. Supreme Court Case No.: 97-1732. [97-2829] [1056207-1] (jame)
10/5/98	Filed order from the Supreme Court GRANTING the Petition for Writ of Certiorari. Supreme Court Case No.: 97-1732. [97-2829] [1105951-1] (heid)

[Filed Jul. 11, 1995—Docketed Jul. 13, 1995]

UNITED STATES DISTRICT COURT
NORTHERN DISTRICT OF ILLINOIS

Civil Action No. 95 C 4006

Jury Trial Demanded

PAUL FELZEN, TRUSTEE OF
LOUISE LASKIN TRUST—1991,
Plaintiff,

v.

DWAYNE O. ANDREAS, RALPH BRUCE, JOHN H. DANIELS, HOWARD G. BUFFETT, LOWELL W. ANDREAS, JAMES R. RANDALL, MICHAEL D. ANDREAS, H.D. HALE, O. GLEN WEBB and MARTIN ANDREAS,
Defendants,

-and-

ARCHER DANIELS MIDLAND COMPANY,
a Delaware corporation,
Nominal Defendant.

COMPLAINT

Plaintiff, for its Complaint brought derivatively on behalf of nominal defendant Archer Daniels Midland Company ("ADM" or "the Company"), alleges upon information and belief, *inter alia,* based upon an investigation conducted by and through its attorneys except as to paragraph 6, which is alleged upon knowledge:

NATURE OF THE ACTION

1. This is a stockholder's derivative action brought on behalf of ADM against certain of the Company's present and former officers, directors and employees. Plaintiff complains of a course of conduct by defendants which caused ADM to systematically engage in price-fixing activities in violation of federal antitrust laws, and to fail to disclose information concerning such conduct, in violation of federal securities law.

2. As set forth in greater detail below, this Complaint alleges that the Company, through its officers and directors, has grossly mismanaged and failed to properly supervise its various divisions, employees, and agents and has made decisions relative to the business, operations and corporate governance of the Company itself and its affiliates which have caused and/or threatened to cause substantial losses to the Company and other damages.

3. The entire ADM Board of Directors knew or recklessly disregarded the fact that these violations were taking place. ADM's Board of Directors failed to adequately oversee ADM's officers and employees, failed to prevent their wrongdoing despite ample opportunity to do so, and failed to create a compliance or auditing program to prevent illegal activities or to detect them after they occurred.

4. Because defendants' illegal conduct was discovered by federal law enforcement officials, ADM and certain of its executives have been subjected to an extensive grand jury investigation, and the Company has seen its stock price decline and suffered significant damage to its reputation and goodwill.

JURISDICTION AND VENUE

5. This Court has jurisdiction over this action pursuant to 15 U.S.C. §§ 1, 4, 15, 26, 78n(a) and 78aa,

and 28 U.S.C. § 1331. Venue is proper in this District pursuant to 28 U.S.C. § 1391(b) because a substantial part of the events giving rise to the claims occurred in this District. This action is not a collusive one to confer jurisdiction on a court of the United States which it would not otherwise have.

PARTIES

6. Paul Felzen is a trustee of plaintiff Louise Laskin Trust—1991 (the "Trust"). The Trust owns and at all relevant times herein has continuously owned shares of common stock of ADM. Plaintiff brings this action derivatively on behalf of nominal defendant ADM.

7. Nominal defendant ADM is a public corporation organized under the laws of Delaware with its principal place of business at 4666 Faries Parkway, Decatur, Illinois. ADM is engaged in the business, among other things, of processing and merchandizing agricultural commodities and products. ADM's products include high fructose corn syrup (which is used in soft drinks and other food products), amino acid lysine (which is used as an animal feed supplement), and citric acid (which is used in the pharmaceutical and food and beverage industries). ADM's common shares are registered pursuant to Section 12 of the Securities and Exchange Act of 1934, 15 U.S.C. § 781, and trade on the New York Stock Exchange.

8. For its fiscal year ended June 30, 1994, ADM reported net earnings of more than $484 million on sales of over $11.3 billion. ADM is named as a nominal defendant herein solely in its derivative capacity and this action is brought on its behalf and no claims are asserted against it.

9. Defendant Dwayne O. Andreas is Chairman of the Board and Chief Executive Officer of ADM, and has been a member of ADM's Board of Directors since 1966. In 1994, Dwayne Andreas received from ADM a salary of

$2,972,630 and other annual compensation of at least $198,000.

10. Defendant Ralph Bruce has been a director of ADM since 1980, and is a former Executive Vice President of the Company. In 1994, Bruce received compensation of at least $75,000 from ADM.

11. Defendant John H. Daniels has been a director of ADM since 1957, and is a former Chairman of the Company. In 1994, Daniels received compensation of at least $100,000 from ADM.

12. Defendant Howard G. Buffett, until approximately July 1995, was a director of ADM and a Vice President of the Company.

13. Defendant Lowell W. Andreas has been a director of ADM since 1966, and is a former President of the Company. In 1994, Lowell Andreas received compensation of at least $75,000 from ADM.

14. Defendant James R. Randall is President of ADM and, since 1975, has been a member of the Company's Board of Directors. In 1994, Randall received compensation of at least $1.4 million from ADM.

15. Defendant Michael D. Andreas is Executive Vice President of ADM and Vice Chairman of its Board of Directors. Michael Andreas has been a member of ADM's Board of Directors since 1985. In 1994, Michael Andreas received compensation of at least $942,000 from ADM.

16. Defendant H.D. Hale is Chairman and Chief Executive Office of ADM Milling Co., a subsidiary of the Company, and has been a member of ADM's Board of Directors since 1973. In 1994, Hale received compensation of at least $800,000 from ADM.

17. Defendant O. Glen Webb is Chairman of the Board and President of ADM/Growmark, a subsidiary of ADM, and has been a member of ADM's Board of Di-

rectors since 1991. In 1994, Webb received compensation of at least $75,000 from ADM.

18. Defendant Martin Andreas is Senior Vice President of ADM and Executive Assistant to the Chief Executive Officer, and has been a member of ADM's Board of Directors since 1986.

19. Each of the foregoing individual defendants, because of his position as an officer and/or director of ADM, owes fiduciary duties to the Company and its stockholders in connection with the operations, management and supervision of the Company. As officers and/or directors of a publicly held company whose stock is registered with the Securities and Exchange Commission under the Securities and Exchange Act of 1934, the individual defendants had a duty to disseminate accurate and truthful information promptly with respect to the Company's operations and management, so that the market price of ADM securities would be based on truthful and accurate information and to insure that the Company's business was conducted in accordance with federal and state law.

20. The individual defendants participated in the wrongdoing complained of herein in order to (i) continue and prolong the illusion of ADM's ongoing growth and profitability and its success as a market leader in the agricultural products business, (ii) inflate the price of ADM's common stock, (iii) conceal the adverse facts concerning ADM's illegal conduct, lack of adequate internal controls, and management and future prospects, and (iv) protect and perpetuate their directoral or executive positions and the substantial compensation and prestige they obtained thereby.

CAUSE OF ACTION

21. Plaintiff repeats and reallages [*sic*] each of the foregoing allegations as if set forth fully herein.

22. ADM is currently the target of a Chicago-based federal grand jury investigation into what the Company has publicly termed "possible violations of federal antitrust laws and related crimes in the food additives industry."

23. The criminal probe, which is focusing on ADM's pricing activities with respect to high fructose corn syrup, amino acid lysine, and citric acid, has been substantially aided by the efforts of an inside "whistle-blower"—ADM's BioProducts Division president, Mark E. Whitacre, who, armed with FBI-supplied tape equipment, has helped federal investigators secretly record conversations and meetings between ADM's representatives and its competitors reflecting price fixing activities violative of federal antitrust law.

24. Federal investigators have also issued subpoenas, and obtained a search warrant, to obtain from the Company additional information concerning its illegal pricing practices. Additional subpoenas have been served upon ADM executives and managers as well as certain of the Company's competitors.

25. Neither these pricing practices nor any information concerning the practices was disclosed by ADM in its Proxy Statement dated September 14, 1994, which the Company's directors, including the individual defendants herein, caused ADM to publicly disseminate to ADM's shareholders in order to solicit votes for the election of ADM directors, including the individual defendants herein. The absence of such disclosure rendered the statements contained in the Proxy Statement materially misleading, in violation of Section 14(a) of the Securities and Exchange Act of 1934, 15 U.S.C. § 14n(a), and the rules promulgated thereunder by the Securities and Exchange Commission.

26. Each of the individual defendants owed ADM and its stockholders fiduciary duties of care, candor and loy-

alty and the duty to exercise, in the performance of their responsibilities as directors, reasonable care in the oversight and supervision of ADM's corporate affairs and management. The individual defendants violated those duties through their conflicting interests, lack of independence and intentional or reckless acts which caused or contributed to the commission of the conduct complained of herein in violation of Section 1 of the Sherman Antitrust Act, 15 U.S.C. § 1, and Section 14(a) of the Securities and Exchange Act of 1934, 15 U.S.C. § 78n(a), and the rules promulgated thereunder by the Securities and Exchange Commission.

27. Based on the foregoing, the individual defendants have violated their fiduciary duties of care, loyalty, reasonable inquiry, oversight, good faith and supervision.

28. The individual defendants knowingly or recklessly caused ADM to engage in the wrongful conduct described herein, or were reckless or grossly negligent in failing to prevent ADM from engaging in such conduct and to ascertain and avert such misconduct.

29. The individual defendants' breaches of fiduciary duty have proximately caused ADM to suffer damages in an amount yet to be determined.

30. Plaintiff has no adequate remedy at law.

31. Plaintiff has not made a demand on ADM's board of directors to pursue the claims herein, because such a demand would have been a futile act for the reasons set forth below:

(a) The board itself is accused of a breach of its fiduciary duties and its members are implicated in and liable for abdicating their responsibility to the Company and its shareholders and for failing to put into place adequate internal controls and means of supervision to prevent the wrongful conduct referred to herein.

(b) A reasonable doubt exists that ADM's directors exercised valid business judgment because the wrongful actions and/or inactions by the individual defendants alleged herein amounted to breaches of their fiduciary duties of good faith, disclosure, due care and loyalty to ADM and its stockholders, and an abdication of the directors' responsibilities giving rise to liability to ADM.

(c) The ADM directors' actions and omissions, which resulted in ADM's improper activities, cannot have been the product of valid business judgment.

(d) At least a majority of the present ADM directors has a disabling conflict by virtue of their personal liability as defendants for the damages caused to ADM by their alleged wrongdoing and, therefore, could not be relied upon to reach a truly independent decision as to whether to commence an action against themselves and other persons responsible for the wrongdoing complained of herein.

(e) Each of the directors receives payments, benefits and other emoluments by virtue of his position with the Company. The directors are interested parties and cannot in good faith exercise independent business judgment in determining whether to bring this action against themselves.

(f) As a general matter in recent years, insurance policies covering the liability of an insured's officers and directors purport to exclude legal claims asserted directly by the insured against such persons. To the extent the Company maintains insurance coverage for the liability of any officers or directors and the policy or policies contain the foregoing exclusion, the insurance policy or policies would not protect the officers and directors if the Company asserted a claim directly against such individuals. Thus, there is a substantial disincentive for the directors to bring any action directly against any officers or directors.

WHEREFORE, plaintiff demands judgment as follows:

A. Against each individual defendant and in favor of nominal defendant ADM for the amount of damages sustained by ADM as a result of the wrongful conduct described herein;

B. Requiring the individual defendants and those under their supervision and control, on behalf of ADM and its shareholders, to implement and enforce policies, practices and procedures, including an appropriate anti-trust compliance program, designed to detect and prevent wrongful conduct of the type described herein;

C. Awarding plaintiff the costs and disbursements of this action, including reasonable attorneys' and experts' fees; and

D. Such other or further relief as the Court deems just and proper.

Plaintiff demands a trial by jury.

Dated: July 11, 1995

[Counsel listing omitted]

[Verification Omitted in Printing]

[Docketed Oct. 31, 1995]

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

[Caption Omitted in Printing]

MEMORANDUM OPINION AND ORDER

Following the public disclosures of the government's criminal antitrust investigation of the Archer-Daniels-Midland Company ("ADM"), ADM has been named as a defendant in numerous civil litigation matters involving both antitrust and securities law allegations. Currently pending before this Court are seventeen cases [1] that have been consolidated before this Court in two consolidated complaints. *In re: Archer-Daniels-Midland, Inc. Securities*

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1 95 C 3979 *EM Lawrence Ltd. v. Archer-Daniels*
95 C 3980 *Madoff v. Archer Daniels, et al.*
95 C 3985 *Castaldo, et al. v. Archer Daniels, et al.*
95 C 4006 *Felzen v. Andreas, et al.*
95 C 4028 *Fuss, et al. v. Archer Daniels, et al.*
95 C 4031 *Gutter v. Archer Daniels, et al.*
95 C 4032 *Pozen, et al. v. Archer Daniels, et al.*
95 C 4036 *Stowers v. Archer Daniels, et al.*
95 C 4037 *Lorber v. Archer Daniels, et al.*
95 C 4041 *Graulich v. Andreas, et al.*
95 C 4091 *Scheniak, et al. v. Archer Daniels, et al.*
95 C 4093 *Seger v. Archer Daniels, et al.*
95 C 4233 *Damaskus v. Archer Daniels, et al.*
95 C 4234 *Fisher, et al. v. Archer Daniels, et al.*
95 C 4535 *Esner v. Andreas, et al.*
95 C 4745 *Cohen v. Archer Daniels, et al.*
95 C 5120 *David Essling Pen.Fd. v. Archer Daniels, et al.*

Litigation, Consolidated Case No. 95 C 3979, generally involves a class action securities action, brought on behalf of plaintiffs who purchased ADM common stock and who allege violations of Sections 10(b) and 20 of the Securities Exchange Act, 15 U.S.C. §§ 78j(b) and 78t(a), and Rule 10b-5 of the Securities and Exchange Commission ("SEC"), promulgated thereunder. This consolidated complaint essentially alleges that during the alleged class period of September 16, 1992, through July 10, 1995, ADM's "earnings and success were driven in large part by the growth of its high fructose corn syrup ("HFCS"), citric acid and lysine production businesses, and also by increased prices for these products." (Cons. Compl. ¶ 7). Plaintiffs specifically allege that, "While the defendants publicly attributed this success to [ADM]'s efficiency and to favorable market conditions, in reality, defendants knew that this was not the case. Rather, [ADM]'s success in the lysine, HFCS and citric acid businesses was possible only because, since at least 1992, ADM had been colluding with its competitors in these markets to fix the worldwide production volume and prices for these products in order to reap illegal and undeserved profits. The defendants concealed this material information from the public in the Company's SEC filings and public announcements in order to inflate artificially the market price of ADM common stock." (*Id.*)

Consolidated Case No. 95 C 4006 makes similar derivative allegations on behalf of plaintiff ADM's shareholders. This complaint specifically alleges that the named director defendants "caused ADM systematically to engage in illegal price-fixing activities involving several of its major products in violation of the federal antitrust laws." (Cons. Compl. ¶ 1).

At this initial point in this securities litigation, this Court has been called upon to determine the proper venue for all future proceedings in both consolidated cases. The

defendants in both consolidated actions have filed a motion, pursuant to 28 U.S.C. § 1404(a), to have these actions transferred to the United States District Court for the Central District of Illinois for further consolidation with three other separate actions currently pending in that district. For the reasons that follow, defendants' motion to transfer venue of the two consolidated cases is granted.

ANALYSIS

ADM seeks transfer of this action to the Central District of Illinois pursuant to 28 U.S.C. § 1404(a), which states:

> For the convenience of parties and witnesses, in the interest of justice, a district court may transfer any civil action to any other district or division where it might have been brought.

28 U.S.C. § 1404(a). Transfer is appropriate under § 1404(a) where the moving party demonstrates that (1) venue is proper in the transferor district, (2) venue and jurisdiction are proper in the transferee district, and (3) the transfer will serve the convenience of the parties, the convenience of the witnesses, and the interest of justice. *Vandeveld v. Christoph,* 877 F. Supp. 1160, 1167 (N.D. Ill. 1995). In this case, the first two factors are not in dispute. Venue is proper in this forum as well as in the Central District of Illinois, the forum where ADM is located. *See* 15 U.S.C. § 78; 28 U.S.C. § 1391(b) and (c). Thus, this opinion focuses on the third factor—whether a transfer will serve the convenience of the parties, the convenience of the witnesses, and the interest of justice.

In evaluating the convenience and fairness of transfer under § 1404(a), the Court must consider both the private interests of the parties and the public interest of the Court. Private interests include: (1) plaintiff's choice

of forum, (2) the situs of material events, (3) the relative ease of access to sources of proof in each forum including the court's power to compel the appearance of unwilling witnesses at trial and the costs of obtaining the attendance of witnesses, (4) convenience to the parties—specifically, their respective residences and abilities to bear the expense of trial in a particular forum. *See Van Holdt v. Husky Injection Molding Systems, Ltd.*, 887 F. Supp. 185, 288 (N.D. Ill. 1995); *G. H. Miller & Co. v. Hanes*, 566 F. Supp. 305, 307 (N.D.Ill. 1983); 15 C. Wright, A. Miller & E. Cooper, *Federal Practice* §§ 3849-53 (1986). Public interest factors include the court's familiarity with applicable law, the desirability of resolving controversies in their locale and the principle that "related litigation should be transferred to a forum where consolidation is feasible." *Coffey v. Van Dorn Iron Works*, 796 F.2d 217, 221 (7th Cir. 1986). *See Van Gelder V. Taylor*, 621 F. Supp. 613, 619 (N.D. Ill. 1985). A party seeking a § 1404(a) transfer bears the burden of showing that "the transferee forum is clearly more convenient" than the transferor forum. *Heller Financial, Inc. v. Midwhey Powder Co., Inc.*, 883 F.2d 1286, 1293 (7th Cir. 1989).

There is no dispute in this case that defendant ADM is a public corporation organized under the laws of Delaware with its principal place of business at 4666 Faries Parkway, Decatur, Illinois. ADM is engaged in the business of, among other things, processing and merchandising agricultural commodities and products. ADM's three main products are high fructose corn syrup (which is used in soft drinks and other food products), amino acid lysine (which is used as an animal feed supplement), and citric acid (which is used in the pharmaceutical and food and beverage industries). All of ADM's executive officers have their offices in Decatur. (Schmalz Dec., ¶ 3). Three of the four meetings per year of ADM's Board of Directors take place in Decatur. (*Id.*, ¶ 4). ADM's central

recordkeeping, its corporate records, and its central computer operations are located in Decatur. (*Id.*, ¶ 7).

On June 28, 1955, ADM publicly disclosed that three separate grand juries, currently sitting in Chicago, San Francisco and Atlanta, are investigating ADM's corporate officers' possible violations of federal antitrust laws. These three grand jury investigations have apparently been topically divided by the Justice Department to coincide with the three main products sold by ADM: lysine, citric acid and high fructose corn syrup.

In evaluating the convenience and fairness of tranfer under § 1404(a), the Court has carefully considered both the private interests of the parties and the public interest of the Court. This Court's evaluation of all the relevant factors under 28 U.S.C. § 1404(a) has led it to conclude that a transfer of these two consolidated cases to the Central District of Illinois is appropriate in this case. The Court's evaluation of each of these factors follows:

A. *Plaintiff's Choice of Forum*

This Court has already noted on numerous occasions that plaintiff's choice of forum has diminished in significance since the enactment of § 1404(a). *Van Holdt v. Husky Injection Molding Systems, Inc.*, 887 F. Supp. at 188. Moreover, the weight to be given to plaintiff's choice of forum is lessened if the chosen forum has relatively weak connections with the operative facts giving rise to the claim. *Id.* In this case, the parties have little or no real connection to this district. The plaintiffs only real connection to this district is that their attorneys happen to have offices in Chicago. However, the convenience to plaintiffs' counsel is not a proper consideration. *Id.* at 190; *Sypert v. Miner*, 266 F.2d 196, 199 (7th Cir.), *cert. denied*, 361 U.S. 832 (1959); *Koos, Inc. v. Performance Industries, Inc.*, 747 F. Supp. 487, 490.

Consolidated Case No. 3979 lists twenty-one different plaintiffs. (Cons. Compl. ¶ 11). However, there is no indication that these plaintiffs are residents of this district. Consolidated Case No. 95 C 4006 lists two plaintiffs. Plaintiff Paul Felzen is a trustee of plaintiff Louise Laskin Trust—1991, which is located in the State of Florida. (Cons. Compl. ¶ 12). The other plaintiff, Sandra Esner, is a resident of the Commonwealth of Pennsylvania. Cons. Compl. ¶ 13).

The Court's review of the plaintiffs' choice of forum leads it to conclude that this factor favors the transfer of this case to the defendants' home district which has a more substantive relationship to this cause of action.

B. *Situs Of Material Events*

This Court especially reviews the situs of material events in deciding a motion to transfer venue to determine whether a lawsuit has any material relationship to this district. The Court's review of this factor strongly favors the transfer of this case. The consolidated securities complaint principally alleges omissions of material information related to alleged criminal antitrust which should have been made by ADM. The consolidated derivative complaint alleges that ADM's directors breached duties to ADM by failing to supervise its employees in a manner which would have prevented their alleged criminal antitrust violations.

Because ADM's headquarters are in Decatur, ADM's Board of Directors meets in Decatur for three of its four yearly meetings; and all of ADM's executive offices are located in Decatur. This Court, therefore, concludes that the Central District of Illinois is the situs of events giving rise to the two consolidated complaints currently pending before this Court. Moreover, ADM's divisions that produce the three products which are the subject of the three pending grand jury investigations are headquartered in

Decatur. The Court's careful review of the two consolidated complaints gives this Court no reason to believe that any material events related to this litigation occurred in the Northern District of Illinois. At best, the consolidated derivative complaint obliquely states that: "[m]any of the acts and transactions giving rise to the violations complained of herein, including the preparation and dissemination to the investing public of false and misleading information, occurred in the District." (Cons. Compl. ¶ 11). However, this broad allegation would also apply to the Central District of Illinois as well as many other federal districts where the alleged international criminal antitrust conspiracy occurred. Given the undisputed facts of this case, which include the unassailable fact that ADM's offices and operations are headquartered in Decatur, this Court concludes that its consideration of the material situs of these consolidated complaints strongly favors a transfer of this case to the Central District of Illinois.

C. *Convenience of the Witnesses and Parties*

The Court next examines the convenience of the witnesses and parties. The Court must determine the relative ease of access to sources of proof in each forum. ADM submits that since all of its offices and relevant employees are in Decatur, this factor weighs heavily in their favor. The plaintiffs have not and can not rebut this fact. Instead, plaintiffs merely allege that Chicago is a more convenient transportation point than the Central District of Illinois. The plaintiffs have not specified any witnesses who may be unavailable in the Central District of Illinois. This Court therefore concludes that the convenience of witness factor favors the transfer of this case to the Central District of Illinois.

The plaintiffs strongly rely on the fact that the grand jury which is investigating possible criminal antitrust activities in the lysine market is located in Chicago. The

Court specifically finds that this fact does not justify venue of these two consolidated securities cases in this district. First, this Court recognizes a clear distinction between the legal issues involved in the criminal antitrust investigation and the legal issues in these two consolidated civil securities cases. While there may be some factual overlap between the factual investigation of this criminal grand jury and the litigants' efforts in these consolidated securities cases, this overlap does not translate into any conveniences for the witnesses in this litigation because it is highly unlikely that there will be any workable coordination between the criminal and civil investigations. In fact, it is highly likely that no effective civil discovery can proceed until the Department of Justice concludes its criminal investigations. Furthermore, the fact that the Chicago grand jury is only investigating one of ADM's three major product lines further diminishes the likelihood that any effective coordination can occur between the two consolidated cases and the criminal grand jury sitting in Chicago.

Finally, in plaintiffs' last-ditch efforts to convince this Court that venue is appropirate in this district they have noted that: (1) one of the key witnesses in this litigation who formerly worked for ADM, Mark Whitacre, is presently working in the Northern District of Illinois and (2) ADM has filed a brief with the Multi-District Litigation ("MDL") Panel which concedes that the civil antitrust MDL cases involving the lysine product should be transferred to the Northern District of Illinois. Neither of these two arguments, when closely examined are persuasive to the Court.

With respect to Mark Whitacre, the plaintiffs have not asserted that his testimony will not be available to them in the Central District of Illinois. In fact, the probability is that Mr. Whitacre will never testify in any of the civil cases and that the parties will instead rely on any testimony offered by Mr. Whitacre in any public criminal

proceedings that may occur in the future. Moreover, there is no guarantee that Mr. Whitacre will be a resident of this district if and when these two consolidated civil actions reach the trial stage.

The Court also believes that ADM's recent MDL pleading, which relates to numerous related civil antitrust cases, does not change its analysis under the venue factors which must be considered by the Court. The Court's close review of this MDL pleading indicates that ADM has essentially never wavered from its position that most of its civil litigation should proceed in the Central District of Illinois. In this MDL pleading, ADM merely has decided that it should follow the same strategic decision of the Justice Department and similarly urge a separate consolidation of all civil antitrust cases along its three separate product lines. Given this strategy, it is not surprising at all that ADM in its MDL filing seeks to have the citric acid and/or HFCS antitrust actions consolidated in the Central District of Illinois. In view of this request and to preserve the separate integrity of the HFCS and lysine cases, ADM reluctantly supported the transfer of all lysine civil antitrust to this district after initially requesting that these lysine cases be sent to the Central District of Illinois. Thus, this MDL filing, when viewed in its proper context, does not suggest or concede that this district is the proper venue for the consolidated litigation pending before this Court. In fact, factual information contained in this MDL pleading merely reiterates that the three products at issue in the related criminal and civil litigation are principally manufactured in the Central District of Illinois. Thus, the Court's own objective review of ADM's MDL pleading leads the Court to conclude that this MDL pleading supports, rather than weakens, ADM's motion to transfer venue of these two consolidated cases to the Central District of Illinois.

C. *The Overall Interests of Justice*

Finally, the Court has independently reviewed whether the overall interests of justice would be served by a transfer of venue. All of the factors reviewed to this point compel the transfer of the venue to the Central District of Illinois, the district having the most meaningful relationship to these two consolidated actions. Here, the overall interests of justice certainly favor a transfer to the Central District of Illinois to facilitate further consolidation with similar cases now pending there.[2] *Coffey v. Van Dorn Iron Works*, 796 F.2d 217, 221 (7th Cir. 1986).

The plaintiffs' main argument against the transfer of these two consolidated cases is that ADM will secure some sort of "home-court" advantage. This argument asserts too much. If the Court was to accept the logic of this argument our American system of jurisprudence would completely breakdown. The essence of the plaintiffs' assertion is that they will not be able to receive a fair trial, if these consolidated cases ever reach that stage, in ADM's home district. The fallacy of this assertion has been proven false over and over again by jury verdicts returned against large corporation [*sic*] in their own home districts throughout the history of our jurisprudence. This Court flatly rejects the assertion that its esteemed colleague in the Central District of Illinois will not be able to properly monitor jury selection in a fashion that will ensure that all parties in this case receive a fair trial.

Plaintiffs' allegations of prejudice in the Central District of Illinois are also ill founded. The Danville Division of the Central District of Illinois, in which Decatur

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2 While plaintiffs' counsel asserts that the current plaintiffs in the Central District of Illinois would be willing to accept a transfer to this Court, this factor carries little, if any, weight with this Court because this simply represents an accommodation between plaintiffs' counsel rather than an acknowledgment that venue is improper in the Central District of Illinois.

is located, comprises 12 counties with a population of 679,000. Even if all of ADM's 1,800 employees and their friends, relatives and acquaintances were automatically excluded from the relevant jury pool, it defies reality to believe that eight fair and impartial persons, a typical civil jury of six persons and two alternates, could not be found in Danville to render a decision in this case.

CONCLUSION

This Court finds that these two consolidated actions bear no meaningful relationship to this district and therefore should be transferred to the Danville Division of the Central District of Illinois for further consolidation with the related pending cases in Danville. Defendants' motion for transfer of consolidated cases No. 95 C 3939 and No. 95 C 4006 is granted. All further litigation matters should be brought before the transferee Court.

ENTER:

/s/ Ruben Castillo
RUBEN CASTILLO
United States District Judge

October 31, 1995

[Filed Dec. 27, 1995]

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS

Case No. 95-2279

Honorable Harold A. Baker
Judge Presiding

PAUL FELZEN, TRUSTEE OF LOUISE LASKIN TRUST - 1991 and SANDRA ESNER,
Plaintiffs,

v.

DWAYNE O. ANDREAS, RALPH BRUCE, JOHN H. DANIELS, HOWARD G. BUFFETT, LOWELL W. ANDREAS, JAMES R. RANDALL, MICHAEL D. ANDREAS, H.D. HALE, O. GLENN WEBB, MARTIN ANDREAS, MARGARETTA ROCKEFELLAR, F. ROSS JOHNSON, RAY A. GOLDBERG, GAYLORD O. COAN, JOHN K. VANIER, SHREVE H. ARCHER, JR., M. BRIAN MULRONEY, AND ROBERT S. STRAUSS,
Defendants,

and

ARCHER DANIELS MIDLAND COMPANY,
a Delaware corporation,
Nominal Defendant.

DEFENDANTS' MOTION TO DISMISS THE CONSOLIDATED AND AMENDED DERIVATIVE COMPLAINT OR, IN THE ALTERNATIVE, TO STAY THE ACTION

The undersigned Defendants move to dismiss the Consolidated and Amended Derivative Complaint for failure

to state a claim upon which relief can be granted. In addition, the undersigned Defendants move to dismiss on the ground that the Plaintiffs failed to make the requisite demand on the nominal corporate defendant, ARCHER DANIELS MIDLAND COMPANY, a Delaware corporation, prior to filing their shareholders derivative action. In the alternative, the undersigned Defendants move the Court for a stay of this consolidated action pending resolution of related criminal and civil litigation. The grounds for Defendants' motion are more fully stated in the accompanying Memorandum of Law.

Defendants respectfully request oral argument on this Motion.

WHEREFORE, the undersigned Defendants request this Court to enter an Order dismissing the Consolidated and Amended Derivative Complaint, or, in the alternative, to enter an Order staying the action pending resolution of the related criminal and civil litigation.

/s/ JAMES E. PECKERT
ARCHER DANIELS MIDLAND COMPANY
Its Attorneys

[Counsel Listing Omitted]

/s/ THOM MOSS
Individual Defendants
Their Attorneys

[Counsel Listing Omitted]

[Filed May 17, 1996]

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA DIVISION

[Caption Omitted in Printing]

CONSOLIDATED AND AMENDED DERIVATIVE COMPLAINT

Plaintiffs, by their attorneys, for their Consolidated and Amended Derivative Complaint against defendants, allege on information and belief, except those allegations that pertain to the named plaintiffs and their counsel, which are based on personal knowledge. Plaintiffs' information and belief is based, *inter alia*, on the investigation made by and through their attorneys, as follows:

INTRODUCTION AND OVERVIEW OF ACTION

1. This is a stockholders' derivative action brought on behalf of and for the benefit of Archer-Daniels-Midland Co. ("ADM" or the "Company") against ADM's Board of Directors (the "Director Defendants") for breaches of fiduciary duty, abuse of control, and gross mismanagement. The Director Defendants caused ADM systematically to engage in illegal price-fixing activities involving several of its major products in violation of the federal antitrust laws. On June 28, 1995, the Company disclosed that three grand juries, sitting in Chicago, San Francisco and Atlanta, are investigating its alleged violations of the federal antitrust laws and related crimes in the food additives industry. These investigations are directed towards price-fixing with respect to lysine, citric acid and high fructose corn syrup.

2. Following this public disclosure, the Company, and certain of its directors and executive officers, were named in several securities fraud class action suits, subsequently consolidated in this District and captioned *in re Archer-Daniels-Midland, Inc. Securities Litigation*, Case No. 95-C-3979. The plaintiff shareholders brought these securities actions on behalf of all persons who purchased the common stock of ADM between September 16, 1992 and July 10, 1995 (the "Class Period") alleging that during the Class Period, ADM and its corporate insiders misrepresented the Company's earnings, profitability, results of operations and business prospects as a result of ADM's price-fixing and other unlawful anti-competitive activities.

3. The Company also has been sued by numerous purchasers of lysine, high fructose corn syrup and citric acid in individual and class actions alleging that ADM and other co-conspirators violated the federal antitrust laws when they agreed to fix, stabilize and maintain at artificially high levels the prices for these products.

4. The ongoing investigation of price-fixing followed former ADM senior executive Marc Whitacre's ("Whitacre") disclosure to federal authorities that such practices were encouraged at ADM. Since the price-fixing allegations became public, Whitacre has disclosed further unlawful conduct on the part of ADM, including the deposit of illegal payments to senior officers and managers in foreign accounts as supposed payment of phony invoices. ADM, in turn, has accused Whitacre and others of embezzling that money. Whitacre maintains that these illegal slush funds were authorized by senior executives of the Company, including certain Director Defendants, in an effort to avoid payment of federal income taxes.

5. As a result of ADM's violations of the federal antitrust and securities laws as well as other violations of law, the Director Defendants have exposed ADM to enormous liability for those violations and considerable expense of defending itself. Currently, 85 state and federal

lawsuits by customers and shareholders alike are pending against ADM as a result of the Director Defendants' actions. To date, ADM has agreed to pay $25 million to settle the lysine civil antitrust case. This payment is not covered by any insurance. In fact, the Company recently disclosed that it had reserved $31 million to cover its litigation costs. Plaintiffs, therefore, seek to recover monies to compensate ADM for damages paid or awarded to plaintiffs and the putative classes in both the private antitrust and the securities lawsuits, the costs of defending itself in any criminal and civil actions resulting from its illegal behavior, and for any fines and/or penalties imposed by the federal government for the lilegal price-fixing and violation of other laws. In addition, as a result of the Director Defendants' having caused the Company to engage in the aforementioned unlawful conduct, the Company's goodwill has been impaired and its credit rating lowered. Therefore, the Company has incurred increased costs in raising capital.

6. By reason of their corporate positions and their ability to control the business and corporate affairs of ADM the Director Defendants owed the Company and its stockholders fiduciary obligations of full disclosure, fidelity, trust, and loyalty. The Director Defendants were required to use their ability to manage ADM in a fair, just and equitable manner, as well as to act in furtherance of the best interests of ADM and its stockholders and not in furtherance of their own personal interests or in violation of law. In addition, each of the Director Defendants owed ADM the duty to exercise due care and diligence in the management and administration of the Company's affairs and in the use and preservation of its property and assets. In violation of their fiduciary duties, the Director Defendants permitted the Company to conduct its business in an unsafe, imprudent and illegal manner by pursuing unsound practices, thereby wasting ADM's assets.

7. The Director Defendants ratified and/or endorsed the ongoing violations of law complained of herein and

the conduct of ADM's officers and employees that resulted in those violations. That ratification and/or endorsement involved a knowing and culpable violation of the Director Defendants' obligations as corporate directors, an absence of good faith on their part, and a reckless disregard for their fiduciary duties to the Company and its public shareholders. The Director Defendants were aware of, or pursuant to reasonable inquiry should have been aware of, the ongoing violations of law in which ADM was engaging, the risks of serious injury to ADM as a result of its engaging in those violations of law, and the personal benefits they obtained as a result of causing ADM to engage in price-fixing and other unlawful, anti-competitive activities.

8. As alleged in greater detail in paragraphs 28 and 29 of this Complaint, the Director Defendants are implicated in the wrongdoing and/or controlled by those implicated in the wrongdoing and would reject any demand by plaintiffs that any of the Director Defendants prosecute this derivative action. Therefore, any such demand by plaintiffs would be futile.

JURISDICTION AND VENUE

9. This Court has jurisdiction under 28 U.S.C. § 1332 (a)(1). Plaintiffs and all defendants are residents and citizens of different states. The amount in controversy between the plaintiffs and the defendants exceeds $50,000, exclusive of interest and costs. This is not a collusive action to confer jurisdiction on this Court which it would not otherwise have.

10. Venue is proper in this District. Many of the acts and transactions giving rise to the violations of law complained of herein, including the preparation and dissemination to the investing public of false and misleading information, occurred in this District.

PARTIES

11. Plaintiff Paul Felzen is a trustee of plaintiff Louise Laskin Trust-1991 (the "Trust"), which is located in the State of Florida. The Trust owns, and at all relevant times herein has continuously owned, shares of the common stock of ADM.

12. Plaintiff Sandra Esner, a resident of the Commonwealth of Pennsylvania, owns, and at all relevant times herein has continuously owned, shares of the common stock of ADM.

13. Nominal defendant ADM is a public corporation organized under the laws of Delaware with its principal place of business at 4666 Faries Parkway, Decatur, Illinois. ADM is engaged in the business of, among other things, processing and merchandizing agricultural commodities and products. ADM's products include high fructose corn syrup (which is widely used in soft drinks and other food products), the amino acid lysine (which is used as an animal feed supplement), and citric acid (which is used in the pharmaceutical and food and beverage industries). ADM's common shares are registered pursuant to Section 12 of the Securities Exchange Act of 1934, 15 U.S.C. § 781, and trade on the New York Stock Exchange. ADM is named as a nominal defendant solely in its derivative capacity.

14. Set forth below is information regarding the individual defendants who served, at all times relevant to the claims set forth herein, as officers of ADM and members of ADM's Board of Directors:

(a) Defendant Dwayne O. Andreas ("D. Andreas") was, at all relevant times, Chief Executive Officer of ADM and Chairman of the Company's Board of Directors. As of September 13, 1995, D. Andreas was the beneficial owner of 23,855,393 shares of ADM common stock, more than 4.7 percent of the total shares outstanding. For the fiscal year ended June 30, 1995, D. Andreas received

salary and other compensation, including stock options, of approximately $3,764,841.

(b) Defendant Michael D. Andreas ("M.D. Andreas") was, at all relevant times, Executive Vice President of ADM and Vice-Chairman of the Company's Board of Directors. M.D. Andreas directly participated in ADM's antitrust violations and is a prime target of the government's investigation. As of September 13, 1995, M.D. Andreas was the beneficial owner of 6,032,157 shares of ADM common stock, 1.1 percent of the total shares outstanding. For the fiscal year ended June 30, 1995, M.D. Andreas received salary and other compensation from ADM of approximately $1,196,004, plus options to purchase 60,000 shares of ADM common stock at $16.8333 per share.

(c) Defendant James R. Randall ("Randall") was, at all relevant times, President of ADM and a member of the Company's Board of Directors. As of September 13, 1995, Randall was the beneficial owner of 1,089,116 shares of ADM common stock, .20 percent of the total shares outstanding. For the fiscal year ended June 30, 1995, Randall received salary and other compensation from ADM of approximately $1,686,004, plus options to purchase 75,000 shares of ADM common stock at $16.8333 per share.

(d) Defendant Ralph Bruce ("Bruce") was, at all relevant times, a director and was also a former Executive Vice President of ADM. As of September 13, 1995, Bruce was the beneficial owner of 263,102 shares of ADM common stock.

(e) Defendant John H. Daniels ("Daniels") was, at all relevant times, a director and a former Chairman of ADM's Board of Directors. As of September 13, 1995, Daniels was the beneficial owner of 461,114 shares of ADM common stock, .09 percent of the total shares outstanding.

(f) Defendant Lowell W. Andreas ("L. Andreas") was, at all relevant times, a director and a former President of ADM. As of September 13, 1995, L. Andreas was the beneficial owner of 6,081,364 shares of ADM common stock, 1.20 percent of the total shares outstanding.

(g) Defendant John K. Vanier ("Vanier") was, at all relevant times, a Director of the Company. As of September 13, 1995, Vanier was the beneficial owner of 9,083,674 shares of ADM common stock, 1.80 percent of the total shares outstanding.

(h) Defendant Martin L. Andreas ("M.L. Andreas") was, at all relevant times, Senior Vice President and a Director of the Company. As of September 13, 1995, M.L. Andreas was the beneficial owner of 1,471,849 shares of ADM common stock, .29 percent of the total shares outstanding. For the fiscal year ended June 30, 1995, M.L. Andreas received salary and other compensation, including stock options, of approximately $1,202,004.

(i) Defendant M. Brian Mulroney ("Mulroney") was, at all relevant times, a Director of the Company. As of September 13, 1995, Mulroney was the beneficial owner of 511 shares of ADM common stock.

(j) Defendant H.D. Hale ("Hale") was, at all relevant times, a Director of the Company and Chairman and Chief Executive Officer of ADM Milling Co., a subsidiary of the Company. As of September 13, 1995, Hale was the beneficial owner of 13,794,268 shares of ADM common stock, 2.70 percent of the total shares outstanding. For the fiscal year ended June 30, 1995, Hale received salary and other compensation, including stock options, of approximately $953,521.

(k) Defendant O. Glen Webb ("Webb") was, at all relevant times, a Director of the Company and Chairman and Chief Executive Officer of Growmark, Inc., a farmer-owned cooperative partly owned by ADM. As of September 13, 1995, Webb was the beneficial owner of 2,029,046 shares of ADM common stock, .40 percent of the total shares outstanding.

(l) Defendant F. Ross Johnson ("Johnson") was, at all relevant times, a Director of the Company. As of September 13, 1995, Johnson was the beneficial owner of 132,331 shares of ADM common stock, .03 percent of the total shares outstanding.

(m) Defendant Shreve M. Archer ("Archer") was, at all relevant times, a Director of the Company. As of September 13, 1995, Archer was the beneficial owner of 1,426,746 shares of ADM common stock, .25 percent of the total shares outstanding.

(n) Defendant Ray A. Goldberg ("Goldberg") was, at all relevant times, a Director of the Company. As of September 13, 1995, Goldberg was the beneficial owner of 544 shares of ADM common stock.

(o) Defendant Robert S. Strauss ("Strauss") was, at all relevant times, a Director of the Company. As of September 13, 1995, Strauss was the beneficial owner of 33,487 shares of ADM common stock.

(p) Defendant Margaretta Rockefeller ("Rockefeller") was, at all relevant times, a Director of the Company. As of September 13, 1995, Rockefeller was the beneficial owner of 13,216 shares of ADM common stock.

(q) Defendant Howard G. Buffett ("Buffett") was, at all relevant times until his resignation in July, 1995, a Director of the Company.

15. Common stock beneficially owned by all directors and executive officers as a group is 72,653,139 shares representing 14.39% of the outstanding shares.

THE DUTIES OF THE ADM DIRECTORS AND OFFICERS

16. Each of the Director Defendants owed the Company and its shareholders the duty to exercise a high degree of care, loyalty and diligence in the performance of his or her individual responsibilities with respect to the management and administration of the affairs of ADM, as well as in the use and preservation of its property and assets. Each of the Director Defendants approved and/or ratified anti-competitive activities and illegal foreign payments. The conduct of the defendants complained of herein involved, *inter alia,* the following: (a) knowing and culpable violation of their obligations as directors and/or officers of ADM; (b) the absence of good faith on their part; and (c) a reckless disregard for their duties to the Company and its shareholders of which the defendants were aware, or should have been aware, that caused serious injury to the Company, allowed these defendants to obtain personal benefits, and subjected the Company to substantial legal exposure.

17. To discharge their legal duties, the Director Defendants were required to exercise reasonable and prudent supervision over the Company's management, policies, practices, controls, and financial affairs. Pursuant to their fiduciary obligations, the Director Defendants are required to use the same care and diligence as would an ordinary prudent person in a similar position. By virtue of this obligation, these defendants were required, but failed among other things:

(a) to undertake a proper and adequate investigation and evaluation of the Company's: (1) product pricing activities to ensure that ADM was not violating the federal antitrust laws; (2) dissemination of information to the public to ensure that ADM was not violating the federal securities laws; and (3) management structure to prevent monies from being improperly removed from the Company to its officers for inappropriate and illegal activities. As a result of the Director Defendants' failure to undertake a proper and adequate investigation and evaluation of these issues, they caused the Company to incur costs of at least $25 million with respect to the settlement of the lysine antitrust action plus attorneys' fees and other costs of defense incurred to date, and exposed it to the imposition of additional fines, penalties, substantial attorneys fees, and other damages;

(b) to manage, conduct, supervise, and direct the business and affairs of ADM carefully, prudently and in good faith, in accordance with the laws, rules and regulations of the federal government, State of Illinois, and the Articles and By-Laws of ADM;

(c) to exercise reasonable control and supervision over the officers and employees of ADM;

(d) to exercise reasonable care in drafting, reviewing, proposing, and evaluating the prudence and soundness of policies and practices to be undertaken by ADM;

(e) to establish guidelines and policies to govern adequately the structure and organization of the Company's operations, including its pricing practices, reporting practices and accounting practices and the reporting thereof;

(f) neither to violate, nor knowingly or recklessly to permit any officer, director or employee of ADM to violate, applicable federal, state or local laws, rules and regulations, including the federal and state securities laws, and federal and state antitrust laws;

(g) to maintain a proper division of authority and responsibility among the officers and directors of ADM so as to prevent the dominance of any officer or director, by any other officer or director in the conduct of the business and affairs of ADM;

(h) to become and to remain informed as to how ADM was, in fact, operating to ensure that ADM did not engage in unsafe, imprudent, unsound or illegal practices;

(i) upon receiving notice or information of an unsafe, imprudent, unsound or illegal practice, to make a reasonable investigation in connection therewith and to take steps to correct that condition or practice;

(j) to establish and to maintain systematic and accurate books and records of the business and affairs of ADM and procedures for the reporting of the business and affairs to the Board of Directors and periodically to investigate, or cause an independent investigation to be made of, ADM's books and records;

(k) to maintain and to implement an adequate and functioning system of internal financial, accounting controls and management information systems, such that ADM's assets would be safeguarded, its financial statements and information would be accurately recorded and reported, and corporate managers were, and would be given prompt notice of serious problems or divergences;

(l) to supervise the preparation and filing of any audited financial statements, reports, or other information required by law from ADM, including the Company's Form 10-Ks, Form 10-Qs, annual reports and proxies; and to examine and evaluate any reports of examinations, audits, or other information required by federal or state law concerning the financial condition of ADM and to make full and accurate disclosure of all material facts concerning, *inter alia*, each of the subjects and duties set forth above; and

(m) to refrain from obtaining personal benefit at the expense of ADM and its public shareholders.

18. The defendants participated in the wrongdoing complained of herein to benefit themselves by enabling themselves to become directors and officers of a much

larger public corporation, to create and to perpetuate the illusion of the Company's success, and to inflate the price of its common stock and to conceal the adverse facts concerning ADM's wrongful conduct, management, financial position and future prospects so that they could, *inter alia*: (a) protect and perpetuate their directorial and/or executive positions and increase the substantial compensation, perquisites, business opportunities and prestige they obtained thereby; and (b) inflate the price of the Company's common stock in order to enhance the value of their securities holdings and options. Such participation involved, among other things, planning and creating, or causing to be planned and created, proposing, or causing the proposal of, and authorizing, approving and acquiescing in the wrongful conduct complained of herein.

CONCERTED ACTION

19. Each of the defendants pursued a common course of conduct, acted with, conspired with and aided and abetted one another to accomplish the violations of fiduciary duties complained of herein. The conspiracy, common enterprise and common course of conduct commenced at least by early 1991, and ultimately involved each of the defendants. The purpose and effect of the conspiracy, common enterprise and common course of conduct complained of was, *inter alia*, to cause ADM to expand and grow so that the defendants could control a much larger entity thus allowing them to increase the value of their own investment and protect their own position and compensation. That expansion was accomplished by, among other things, controlling the market for ADM's products through a scheme of price-fixing, and setting up and permitting the use of slush funds for improper and illegal purposes. Each Director Defendant was a direct, necessary and substantial participant in the conspiracy, common enterprise and common course of conduct complained of herein.

20. Each of the defendants named herein aided and abetted and rendered substantial assistance to accomplish the violation of fiduciary duties. In taking the actions, to aid and abet and substantially assist the violation of fiduciary duties complained of, each defendant acted with an awareness of the wrongdoing and realized that his or her conduct would and did substantially assist the violations complained of.

21. As members of ADM's Board of Directors or management, the defendants were themselves directly responsible for failing to monitor or for authorizing or permitting the authorization of ADM's price-fixing activities and use of illegal slush funds. Each of them had knowledge of and actively participated in and approved of the wrongdoing and/or abdicated his or her responsibilities with respect to the wrongdoing. The alleged acts of wrongdoing were committed outside of standard, accepted corporate practices and have subjected ADM, to date, to a loss in excess of $25 million.

22. Each of the defendants is liable as a direct participant in, an aider and abettor of, and/or a co-conspirator with respect to the violations of fiduciary duties and had the power and influence to cause, and did cause, ADM to engage in the conduct complained of herein.

DERIVATIVE ALLEGATIONS AND DEMAND FUTILITY

23. Plaintiffs bring this action derivatively in the right of, and for the benefit of, ADM to redress injuries suffered and to be suffered by ADM. These injuries are the direct result of the breaches of fiduciary duties, corporate mismanagement and abuses of control which led to violations of federal and state law.

24. Plaintiffs will adequately and fairly represent the interests of ADM and its shareholders in enforcing and

prosecuting their rights and have obtained counsel competent and practiced in litigating derivative actions.

25. There were sixteen (16) ADM directors on the Board on July 11, 1995, the date this derivative action was initially filed. Those directors were: Dwayne O. Andreas, Lowell W. Andreas, Michael D. Andreas, Martin Andreas, John H. Daniels, Jamie R. Randall, H.D. Hale, O. Glenn Webb, Ray A. Goldberg, John K. Vanier, Ralph Bruce, Shreve M. Archer, Jr., F. Ross Johnson, M. Brian Mulroney, Robert S. Strauss, and Margaretta Rockefeller. Prior to July 11, 1995, Howard G. Buffett publicly announced he had resigned; he was subsequently replaced by G.O. Coan.

26. Because a majority of the ADM Board was not disinterested and independent, and was therefore unable to objectively decide the merits of plaintiffs' claims, demand on the Board would have been futile, and is therefore excused.

27. Any demand made by plaintiffs to the ADM Board to institute this action is excused under Rule 23.1 of the Federal Rules of Civil Procedure. Such demand would be a futile and a useless act for the following reasons:

A. A Majority Of The Board Is Interested And/Or Lacks Independence

28. For the reasons set forth herein, a majority of ADM's directors are interested and/or are controlled and dominated by defendants D. Andreas, M.D. Andreas and Randall (the "Controlling Directors") each of whom is an interested director. Furthermore, because defendants D. Andreas, M.D. Andreas and Randall are interested and are Controlling Directors, the remaining directors could not exercise their independent judgment with respect to any demand made on the Board.

(a) Defendant D. Andreas, as Chief Executive Officer of ADM and Chairman of the Board of Directors is in fact an interested director. Moreover, because he is a Company insider he is, by legal definition, not disinterested and independent. In addition, through his actions, defendant D. Andreas controls and dominates the Board of Directors as follows:

(1) D. Andreas controlled and dominated the process by which each defendant director was selected for nomination or renomination to the ADM Board. D. Andreas and M.D. Andreas control the four members of the Board's nominating committee. Non-employee directors are paid an annual retainer fee of up to $100,000, more than twice the industry norm. Each defendant director therefore had a direct economic incentive to please D. Andreas and his top officers in order to stay on the Board of Directors.

(2) D. Andreas' ability to handpick his directors and control the Board is widely recognized. As a result of his ability to control and dominate the Board, D. Andreas was able to "stuff[] his board with family and friends and company officers and paid them more than twice the norm [to serve as ADM directors]." "Corporate Governance's Sorry History," *The Wall Street Journal*, April 18, 1996 page C2 column 3. By handpicking relatives, friends and ADM officers as ADM directors, D. Andreas has maintained complete control over the ADM Board of Directors. The ADM Board does nothing that D. Andreas does not want it to do including, causing the Company to engage in anti-competitive practices.

(3) D. Andreas' contempt for ADM's shareholders is evident. At its October 19, 1995, annual shareholders' meeting, D. Andreas displayed his lack of regard for the interests of ADM's shareholders by "shout[ing] down shareholders and order[ing] the audience microphones

turned off." When a pension plan official exclaimed, "this is telling us a lot about how this company is run," D. Andreas responded "[t]his meeting, sir, runs according to *my* rules." "A Grain Of Activism At Archer Daniels Midland," *Business Week*, November 6, 1995 p. 44 (emphasis added). According to Dain Bosworth analyst Bonnie Wittenberg, ADM has "a corporate culture problem." "The ADM Tale Gets Even Stranger", *Fortune*, May 13, 1996, p. 113.

(4) As a result of D. Andreas' dominating position, ADM has been called "a public company that has been run as a family fiefdom." As Richard H. Koppes, deputy executive director of the California Public Employees' Retirement System (CalPERS), stated, the ADM Board needs a majority of "truly independent directors." For years, D. Andreas and ADM have ignored critics of their "insider-dominated" Board. CalPERS, prior to ADM's October 19, 1995 annual meeting, gave ADM the grade of "F" for ADM's failure even to respond to CalPERS's corporate governance queries. "A Grain Of Activism At Archer Daniels Midland," *Business Week*, November 6, 1995, p. 44.

(5) D. Andreas' business philosophy is "[t]he competitor is our friend, and the customer is our enemy." Because of D. Andreas' strong convictions he could and did succeed in causing the Board to approve of ADM's anti-competitive behavior which is now the subject of three grand jury investigations and numerous civil antitrust lawsuits. These facts indicate that defendant D. Andreas not only dominates and controls the Board but imposes a corporate policy that considers the shareholders of the Company children who should be seen and not heard. The Board and the Company is truly his fiefdom.

(b) Defendant M.D. Andreas, as executive vice president of ADM, Vice-Chairman of the Board of Directors and the son of D. Andreas, is in fact an interested direc-

tor. Moreover, because he is a Company insider he is, by legal definition, not disinterested and independent. In addition, M.D. Anreas directly paritcipated in ADM's antitrust violations and is a prime target of the government's investigation. Defendant M.D. Andreas, through his actions and position with the Company, including his position on the Board's nominating Committee, controls and dominates the Board of Directors.

(c) Defendant Randall, as president of ADM, is in fact an interested director. Moreover, because he is a Company insider he is, by legal definition, not disinterested and independent. In addition, defendant Randall has been directly implicated in ADM's antitrust violations and is a prime target of the government's investigation. Defendant Randall, through his actions and position with the Company, controls and dominates the Board of Directors.

(d) Defendant M.D. Andreas, as senior vice president of ADM, is in fact an interested director. Moreover, because he is a Company insider he is, by legal definition, not disinterested and independent.

(e) Defendant Hale is Chairman and CEO of ADM Milling Co., an ADM subsidiary. Hale is the fourth most highly paid ADM officer. By virtue of his executive position with the Company's subsidiary, he is an insider and, by legal definition, is not disinterested and independent.

(f) Defendant Webb is the Chairman and Chief Executive Officer of Growmark, Inc., a farmer-owned cooperative partly owned by ADM. Growmark, Inc. sells approximately one billion bushels of grain annually to ADM and owns approximately 2,025,600 shares of ADM stock. Defendant Webb is also Chairman of ADM/Growmark River Systems, Inc. Because of Webb's positions at the Growmark entities, which are closely tied financially to ADM, he is not disinterested and independent.

(g) Defendant Mulroney, a long time friend of defendant D. Andreas, is a senior partner in the law firm Ogilvy Renault, which has been retained in the past by ADM and received substantial fees for services rendered to ADM. Because of Mulroney's financial interest in his law firm's receiving legal fees and expecting to render legal services to ADM in the future, he is not disinterested and independent. In addition, while Mulroney was Canadian Prime Minister, the Canadian Bureau of Competition Policy, in two controversial decisions, first blocked the merger of two Canadian flour millers (who competed with ADM) and then allowed ADM to buy one of those millers.

(h) Defendant Strauss, is a named partner in the Washington, D.C. law firm Akin, Gump, Strauss, Hauer and Feld, which not only identified and turned in Mark E. Whitacre, but has continuously provided legal services to ADM and received substantial legal fees throughout the relevant period. Because of Straus' [*sic*] financial interest in his firm's having received legal fees in the past and expecting to render legal services to ADM in the future, he is not disinterested and independent. According to news reports, defendant Strauss told the Washington *Post*: "Dwayne Andreas just owns me . . . He captures the imagination of everybody he touches . . . My God, he's the ablest man in America." *Fortune*, August 21, 1995, p. 59.

(i) Defendant L. Andreas, a former president of ADM, is the brother of defendant D. Andreas, and the uncle of M.D. Andreas and M.L. Andreas. Because of his family relationship with these defendants, who all have disabling interests, defendant L. Andreas is controlled and dominated and, therefore, lacks any independence.

(j) Defendant Vanier, the brother-in-law of defendant Hale, has a beneficial interest in farms and ranches that sold $584,568 worth of crops to ADM during the fiscal

year ending June 30, 1995. Vanier is not disinterested because of his financial stake in continuing to do business with D. Andreas and ADM. In addition, because of his familial relationship with Hale, defendant Vanier is controlled and dominated and, therefore, lacks any independence.

(k) Defendant Archer is the father of C.P. Archer, an ADM insider by virtue of his position as company treasurer. Because of his close relationship with a corporate officer whose position is dependent on the controlling directors, D. Andreas, M.D. Andreas and Randall, defendant Archer is controlled and dominated and, therefore, lacks any independence.

(l) The remaining directors, Bruce, Rockefeller, Goldberg, Daniels, and Johnson are all longtime friends and colleagues of D. Andreas and each lacks any independence since they are controlled by D. Andreas, M.D. Andreas and Randall who each have disabling interests. The domination of the Board of Directors by the Controlling Directors has impaired the Board's ability to exercise its business judgment validly and rendered it incapable of reaching an independent decision as to whether or not to accept plaintiffs' demands.

B. Other Reasons Why The Directors Are Not Disinterested And Cannot Be Objective In Evaluating The Merits Of A Demand

29. Additional reasons for each individual director's lack of independence in considering a demand is by virtue of his or her participation in, approval of, and/or reckless disregard of the alleged wrongdoing. Therefore, each defendant is fatally interested in the outcome of any litigation brought against the ADM Board as a whole. Such profound interest is manifest as follows:

(a) the entire ADM Board of Directors participated in and/or were fully aware of the deliberative process

behind many of the acts of wrongdoing alleged herein. The ADM Board of Directors also either approved of, participated in or recklessly disregarded those instances of wrongdoing;

(b) the acts of wrongdoing, the ratification of which was improper and illegal, constitute violations of the fiduciary duties each ADM director owed to the Company and its shareholders. Therefore, a reasonable doubt exists that the Director Defendants exercised valid business judgment because their wrongful actions and/or inactions amounted to breaches of their fiduciary duties of good faith, disclosure, due care and loyalty to ADM and its shareholders, and an abdication of their responsibilities as directors, which breaches and abdication gave rise to ADM's liability for the illegal wrongdoing;

(c) the members of the ADM Board of Directors, by receiving payments, benefits, stock options and other emoluments by virtue of their positions and control of ADM, have benefited from the wrongdoing and have engaged, authorized and/or covered up such conduct to preserve their positions of control. The Board members also have close personal and business ties with each other as well (as set forth above) and, consequently are interested parties and cannot in good faith exercise independent business judgment to determine whether to bring this action against themselves.

(d) ADM's officers and directors are protected against personal liability for their acts of mismanagement and breach of fiduciary duty by directors' and officers' liability insurance. The Director Defendants caused the Company to purchase that insurance for their protection with corporate funds, *i.e.*, monies belonging to the stockholders of ADM. However, the directors' and officers' liability insurance policies covering the defendants in this case contain an "insured versus insured exclusion," a provision which eliminates coverage for any action brought directly

by ADM against the Director Defendants. As a result, if these directors were to sue themselves or certain of the officers of ADM, or to take over this suit and prosecute it, there would be no directors' and officers' insurance protection. The Director Defendants would subject themselves, their relatives and their friends and colleagues to a judgment in the millions of dollars that would be payable from their individual assets alone. This is a further reason why they will not bring such a suit, or would not prosecute any such action vigorously. On the other hand, if the suit is brought derivatively, as this action is brought, such insurance coverage exists and will provide a basis for the Company to recover for the Director Defendants' wrongdoing.

30. Plaintiffs have made no demand on stockholders of ADM to institute this action because such demand would be a futile and useless act for the following reasons:

(a) ADM is a publicly traded company with many thousands of stockholders;

(b) making demand on such a large number of stockholders would be impossible for plaintiffs who have no way of finding out the names, addresses or phone numbers of stockholders; and

(c) assuming all stockholders could be individually identified, making demand on all stockholders would force plaintiffs to incur huge expenses.

THE SPECIAL COMMITTEE AND CORPORATE GOVERNANCE COMMITTEE OF THE BOARD OF DIRECTORS

The Special Committee

31. The Director Defendants' failure to take any action on behalf of ADM prior to the filing of this derivative action constitutes further evidence that demand is futile. In response to the investigation by the Department of Justice ("DOJ"), the filing of the derivative lawsuits and

the class action lawsuits for violations of the federal securities and antitrust laws, on or about July 19, 1995, ADM's Board of Directors announced the formation of a Special Committee consisting of nine directors—Archer, Bruce, Goldberg, Johnson, Vanier, Webb and Rockefeller, with defendants Mulroney and Daniels as co-chairs. The Special Committee retained the law firm of Simpson, Thacher & Bartlett as counsel.

32. The Special Committee, according to an ADM press release, will "direct the Company's response to matters related to the government investigation of the high-fructose corn syrup, citric acid and lysine industries and certain related civil suits".

33. Professor John Coffee, a noted corporate governance expert at Columbia University Law School, has noted that ADM needs more than a special committee. Instead, Professor Coffee stated, it needs "a team of experts to lead a full-blown *independent* investigation," because "the allegations against ADM could not be more serious." "Checks, Lies and Videotape," *Fortune*, October 30, 1995 p. 109 at 112 (emphasis added).

34. Moreover, for the reasons set forth in paragraphs 28-29 above, the Special Committee is anything but independent. At least three of the directors on the Special Committee, including Mulroney who is a co-chair, have disabling personal and professional ties to D. Andreas. All have direct personal ties to D. Andreas. The members of the Special Committee are "outside directors" only to the extent that they are not employees of ADM. They do not conform to the Council of Institutional Investors definition of outside director, namely, a person whose only tie to the company is his or her directorship.

35. The Special Committee has yet to render its findings and recommendations. Any recommendation, other than one to prosecute each director for breaching his or her fiduciary duties to ADM and its shareholders, would

be a whitewash. Because the Special Committee is composed of interested, non-independent directors who were themselves involved in the alleged wrongdoing, such a recommendation will not be made. For that reason as well, any demand made on ADM's Board of Directors would be futile.

The Corporate Governance Committee

36. On or about October 21, 1995, the Board, in an attempt to muffle institutional shareholders' constant barrage of criticism aimed at the "family" run Board, created the Corporate Governance Committee, co-chaired by defendants Goldberg and Webb, to examine the Board's size, director, qualifications, ethics, compensation and other issues, including whether the Board has sufficient independence from management.

37. On or about January 15, 1996, the Corporate Governance Committee announced its recommendations, which would weaken the control of defendant D. Andreas and force the retirement of several directors with close ties to him. As reported in *The Wall Street Journal* on January 16, 1996, "[t]he committee's report surprised Wall Street because it signaled that *Mr. Andreas, who has run the* [*Company*] *in an autocratic style rare for a publicly traded company* may be bowing to shareholder pressure to overhaul the 17-member board" (emphasis added).

38. The report made several major recommendations with respect to the composition of the new Board, including that an outside director cannot be a current employee, a retired senior executive, the "close" relation of a senior manager, or someone who has a "personal" business or professional relationship with the Company.

39. Notwithstanding these changes, *The Wall Street Journal* stated that "it is far from clear how much influence Mr. Andreas will lose over the Board, *which hasn't seriously challenged his authority since he became chairman in 1972*". The Corporate Governance Committee's report acknowledges, through its recommendations, that the Board was and is completely controlled and dominated by D. Andreas and therefore lacks any true independence.

WRONGDOING BY THE OFFICER AND DIRECTOR DEFENDANTS

40. The Director Defendants, as corporate officers and directors, owed ADM the duty of due care in the performance of their responsibilities with respect to ADM's operations. Each of the Director Defendants in this action, acting individually or jointly, failed to exercise reasonable diligence and due care, was grossly negligent or reckless and committed, *inter alia*, one or more of the following actions or omissions constituting fraud, mismanagement and breaches of fiduciary duty:

(a) the Director Defendants authorized, caused or permitted ADM to engage in illegal activity including the violation of the federal antitrust and securities laws;

(b) the Director Defendants exposed the Company to financial injury by failing and refusing to institute legal action against those officers, directors and employees responsible for the illegal activity and for permitting ADM to engage in the improper, illegal and fraudulent practices described herein;

(c) the Director Defendants failed to take reasonable and adequate steps to preclude, prevent, investigate or correct the occurrence of illegal pricing practices at ADM;

(d) the Director Defendants failed to take reasonable and adequate steps to preclude, prevent, investigate or correct the making of illegal payments to foreign accounts for Company executives;

(e) the Director Defendants authorized, caused or permitted ADM to conduct its business in an unsafe, imprudent manner, concealing the true nature of their illegal

conduct to violate the federal antitrust, securities, and other laws and the likely serious adverse impact on ADM's financial condition and prospects;

(f) the Director Defendants failed to exercise independent judgment in the conduct of ADM's business and abdicated their responsibility for the management and supervision of the Company, allowing themselves to be controlled and dominated by defendant D. Andreas;

(g) the Director Defendants' conduct has damaged ADM by exposing it to the costs of defense and liability for violations of the federal antitrust and securities laws for, at least, $25 million; and

(h) the Director Defendants have damaged the goodwill and reputation of ADM due to the adverse publicity that they have generated by their actions. As a result, the Director Defendants have impaired ADM's ability to raise capital at a reasonable and/or low cost. The Company's credit rating has been adversely affected, and its cost of capital has, therefore, already increased.

BACKGROUND FACTS

41. ADM is a $12 billion corporate empire built, according to defendant D. Andreas, by "developing more expensive products from raw [agricultural] commodities and convincing the world it needed them." ADM's strategy is straightforward: to be a major player in all businesses it enters as well as the lowest-cost producer. ADM is one of the world's largest processors of corn, wheat and oilseeds, as well as a major procurer, transporter, processor and merchandiser of numerous other agricultural products. It has proclaimed itself the "supermarket to the world".

42. Corn refining is ADM's most profitable activity, accounting for approximately 55 to 70 percent of its yearly operating earnings. Among other things, the Company processes corn to produce citric acid and high fructose corn syrup ("HFCS"), which are food additives, and lysine, which is used in livestock feed. The Company's customers include many Fortune 500 companies, including most major United States food manufacturers.

43. ADM's business has grown in recent years driven, in part, by expansion of its HFCS business. The Company's Corn Processing Division, which is run by Terrance S. Wilson ("Wilson"), produces HFCS. HFCS became popular in the 1980s as an alternative to sugar and is used extensively as a sweetener in soft drinks, as well as in cakes, cookie mixes, candy bars and instant breakfast foods. With the recent rise in popularity of iced teas and fruit-flavored drinks, demand for HFCS has increased even more. The Company dominates the United States market for HFCS, maintaining an approximately 30 percent market share.

44. The Company has also experienced rapid growth in its BioProducts division, which was founded in 1989 to produce feed-grade amino acids, vitamins and antibiotics from corn starch and soybean meal. Up until very recently, the President of the BioProducts Division was Mark E. Whitacre ("Whitacre"), who joined the Company in 1989 and was generally considered to be the driving force behind the BioProducts Division's growth, as well as the likely successor to defendant Randall as President of the Company. Today, bioproducts represent approximately 15 percent of the Company's earnings, according to analysts.

45. The most important product of ADM's BioProducts Division is lysine, a corn-derived amino acid which is used in swine and poultry feed to promote the growth of lean muscle in animals. When the Company entered the lysine market in 1989, it was the only American producer of lysine and the market was dominated by two Japanese companies, Kyowa Hakko Kogyo and Ajinomoto. By the end of 1992, however, ADM had doubled its lysine production capacity to 250 million pounds per year, and

today it controls more than 50 percent of the $650 million worldwide market.

46. In addition to lysine, the BioProducts Division has thrived by producing citric acid which, like HFCS and lysine, ADM manufacturers from corn. ADM entered the citric acid market in 1990 through its purchase of a Pfizer, Inc. division. Citric acid is used heavily by the beverage industry as a flavor enhancer. It is also added to jams, jellies and candy to provide tartness; to frozen foods to help prolong shelf life; and to shampoos and hair-care products to control acidity.

ADM'S PRICE-FIXING

47. When ADM began its BioProducts Division in 1989, its objective was to become a world leader in the production of amino acids and other bioproducts. To accomplish that objective, the Company's first goal was to develop lysine "into massive business," as noted by Whitacre in an interview appearing in the September 4, 1995 issue of *Fortune* (the "*Fortune* Interview").

48. In order to develop its lysine business, ADM first attempted a "predatory pricing" strategy that it had previously used successfully. The strategy was to gain customers and market share quickly, even at the initial expense of profitability, by flooding the market with lysine at low prices with the intent that competitors would be driven out of the market. Once the Company had gained market share, it hoped to raise prices and earn profits.

49. This strategy was partially successful and, by 1992, the Company had gained more than thirty percent of the worldwide lysine market. The price war ADM initiated drove lysine prices down from approximately $1.30 pound to $.60 a pound, causing ADM and its competitors to lose millions of dollars every month. However, the keystone of the plan failed in that no competitors dropped out of the business.

50. Unable to make lysine production profitable through predatory pricing, the defendants determined that they could achieve profitability through another method—they would raise lysine prices by convincing ADM's competitors in the lysine business to agree to fix lysine prices at an artificially high level and allocate markets, thus allowing them all to reap undeserved and illegal profits.

51. Such anti-competitive and illegal practices were neither new to ADM, nor unique to its lysine business. As stated by Whitacre in the *Fortune* Interview, illegal price-fixing occurred in "four or five other divisions" and was "fairly common." Thus, prior to and during all times relevant to this Complaint, the Director Defendants and other executives at ADM were illegally fixing the prices and production volumes of citric acid and HFCS. According to Whitacre, defendant M.D. Andreas and other executives often quoted defendant D. Andreas' business philosophy as "the competitor is our friend, and the customer is our enemy."

52. The lysine price-fixing process began around February of 1992 when defendants M.D. Andreas and Randall instructed Whitacre to work more closely with Wilson so that Wilson could teach him some things "about how ADM does business." Wilson was notorious among ADM executives as the person who generally orchestrated the Company's price-fixing activities. As stated by Whitacre in the *Fortune* Interview, he understood Wilson's involvement with lysine to mean that they "were going to do business by the Terry method," meaning fixing the price of lysine with competitors.

53. Whitacre and Wilson met in February, 1992, to discuss the lysine business. During that meeting, Wilson told Whitacre that he wanted to meet with ADM's competitors "because we were losing several million dollars a month." He also told Whitacre "[w]e're not blaming that on you. Obviously we needed to get market share

first, and that's what we did. That was stage one. But now we need to take the business to a different tier."

54. In April, 1992, Whitacre and Wilson held meetings in Tokyo with representatives from ADM's two biggest Japanese competitors in the lysine business, Kyowa Hakko Kogyo and Ajinomoto. The purpose of that meeting was to determine whether their competitors were interested in entering into a conspiracy to fix prices.

55. A few months later, in June, 1992, Wilson and Whitacre again met with ADM's Japanese competitors. During that meeting, Wilson gave a presentation in which he discussed how ADM's entry into the lysine market had resulted in production capacity 20% to 25% greater than current usage levels, and that this overcapacity had resulted in prices being driven down from $1.30 per pound to $.60 per pound. He also explained how this drop in price resulted in a $200 million loss in revenues. He stated: "well, gentlemen, there's $200 million that we're giving to our customers. In other words, the customer is benefitting, not the people who spent hundreds of millions of dollars building these plants." Wilson then repeated the ADM philosophy of "the competitor is our friend, and the customer is our enemy."

56. Over the next several months the Director Defendants authorized, carried out and acceded to a scheme, in conjunction with the Company's competitors in the lysine market, including Kyowa Hakko Kogyo, Ajinomoto and others, to fix the worldwide price and market share of lysine, in violation of the federal antitrust laws.

57. In connection therewith, Whitacre and Wilson, under the direction of defendants M.D. Andreas and Randall, held numerous meetings with ADM's competitors in various locations all over the world. Most of ADM's high-level management were aware of these meetings and what transpired therein. For example, Richard P. Reising, the Company's General Counsel, who sometimes prepare for these meetings, was once quoted as saying to

Whitacre and Wilson as they were departing for a meeting, "Hey, guys, good luck with your price-fixing meeting."

58. During these meetings, the companies entered into collusive, anti-competitive agreements to fix lysine prices and market share worldwide at artificial levels in order to reap illegal profits. For example, one method they used was to set monthly sales targets for each company as a means of artificially limiting supply and thereby maintaining an inflated price. Through these anti-competitive agreements, the Director Defendants caused ADM and the other companies to knowingly violate the federal antitrust laws.

59. Prior to and throughout all times relevant hereto, the Director Defendants caused ADM to engage in collusive, anti-competitive volume and price-fixing schemes and other anti-competitive activities with its competitors in the citric acid and HFCS businesses.

60. With regard to citric acid and HFCS, ADM's illegal activities were also orchestrated by, and with the approval of, ADM's Board of Directors. Wilson attended meetings around the world with senior officials of competing citric acid producers, including Hoffman-LaRoche, Inc. and Bayer AG. During these meetings, the companies entered into collusive, anti-competttiive agreements to fix worldwide citric acid prices and market share at artificial levels.

61. Through these activities, ADM and its competitors were able to fix the worldwide production volumes and prices of citric acid and HFCS at artificial levels, and thus reap illegal profits, in knowing violation of the federal antitrust laws.

THE FEDERAL INVESTIGATION

62. On or about June 27, 1995, agents of the Federal Bureau of Investigation ("FBI") and the Antitrust Division of the DOJ, armed with subpoenas seeking docu-

ments and records regarding the Company's citric acid, HFCS and lysine operations to be used in connection with their investigation of ADM's anti-competitive activities, visited the homes of numerous ADM executives and managers. Several carloads of agents also went to ADM's corporate headquarters.

63. The next day, ADM released a terse, two-sentence statement that a federal grand jury in Chicago was investigating "possible violations of federal antitrust laws and related crimes in the food additives industry." The Company also indicated that it had been served with a search warrant and subpoenas for documents and testimony concerning its marketing practices. The statement failed, however, to disclose the magnitude of the investigation, that it was commenced because of a tip from one of ADM's senior corporate executives, Whitacre, or that the investigation had been on-going since 1992.

64. According to an article published on July 10, 1995, in *The Wall Street Journal*, Whitacre approached the FBI in 1992 after he had been asked by an ADM executive to participate in a pricing arrangement, involving the ADM products lysine and citric acid that he believed was collusive. Whitacre produced information indicating that ADM had engaged, and was engaging, in collusive pricing practices. The *Journal* reported that Whitacre had been an undercover operative for the FBI for the past three years and had secretly assisted the government in making hundreds of tape recordings of ADM's anti-competitive and illegal volume and price-fixing activities.

65. Recently, it was reported in the May 13, 1996 edition of *Fortune*, the DOJ had struck a bargain with another ADM executive who knew about the price fixing of lysine and promised him immunity in exchange for his testimony.

66. In addition, the *Journal* further disclosed that, as a result of the investigation, defendant Buffett had re-

signed from ADM's Board of Directors the prior week "because he was troubled by the investigation and the way the Company was handling it," and because he had "lost confidence in whether he was being accurately informed by other [ADM] executives about the details of the antitrust matter."

67. The price of ADM common stock had dropped approximately 15% from $18.625 per share on June 26, 1995, the day before the FBI entered the corporate offices of ADM and the homes of ADM officers and employees, to $14.28 per share on July 10, 1995, the date on which the *Journal* article was published. As a result of the disclosures and the drop in the price of ADM's stock, several shareholders of the Company filed suits alleging violations of the federal securities laws.

68. In the wake of the announcements regarding the government's antitrust investigations, numerous purchasers of ADM products have filed individual and class civil antitrust suits throughout the country alleging that ADM engaged in illegal anti-competitive practices.

69. Recently, the Company announced that it had entered into a settlement, subject to court approval, of the civil lysine case in which it agreed to pay *$25 million*. This settlement is to be paid directly by the Company and not by any insurance. Additionally, the Company recently disclosed in court papers filed in the lysine case that it had increased its reserve for litigation from $16 million to *$31 million*.

ADM'S SLUSH FUNDS

70. According to Company statements, huge sums of the Company's monies have been paid into foreign bank accounts for the benefit of senior officers and managers of the Company. According to the August 22, 1995 edition of *USA Today*, ADM routinely rewarded top executives with foreign pay deposited in overseas ac-

counts. Whitacre sent a letter to *The Wall Street Journal* that appears to acknowledge that he was the recipient of money from ADM through unusual means. He wrote that "[r]egarding overseas accounts and kick-backs, and overseas payments to some employees, . . . Dig deep. Its there! They give it, then use it against you when you are their enemy." When asked to comment on this allegation, an ADM official declined to comment.

COUNT I

DERIVATIVE CLAIM AGAINST ALL DEFENDANTS FOR INTENTIONAL BREACH OF FIDUCIARY DUTIES

71. Plaintiffs incorporate by reference and reallege paragraphs 1 through 70 above as though set forth fully herein.

72. The Director Defendants are fiduciaries of ADM and all of its public shareholders and owe to them the duty to conduct the business of the Company loyally, faithfully, carefully, diligently and prudently. This count is asserted based upon the Director Defendants' acts in violation of Delaware common law, which acts constitute the intentional breach of fiduciary duty.

73. The Director Defendants, in their roles as executives and directors of the Company, participated in the acts of mismanagement alleged herein, or acted in reckless disregard of the facts known to them, and failed to exercise due care to prevent the Company from engaging in illegal acts, including M.D. Andreas' and Randall's active role in the price-fixing of ADM products, violating the federal securities and antitrust laws and creating slush funds for its top executives. The Director Defendants thereby intentionally and deliberately breached their duties of care, loyalty, accountability and disclosure to the shareholders of the Company by failing to act as an ordinarily prudent person would have acted in a like position.

74. The Director Defendants have been responsible for the gross mismanagement of ADM in connection with the price-fixing of its major products and violations of the federal securities laws. The Director Defendants abdicated their corporate responsibilities, by mismanaging the Company in at least the following ways:

(a) they subjected the Company to a Department of Justice investigation for alleged price-fixing violations of the federal antitrust laws;

(b) they caused the Company to engage in the unlawful price-fixing, which has resulted in numerous private civil antitrust suits throughout the county brought by purchasers of its corn processing products; and which has already resulted in the proposed settlement in the lysine civil case in which ADM agreed to pay $25 million, which will not be paid by any insurance policy;

(c) they concealed from the Company's shareholders and the investing public the true nature and extent of the problems that the Company was suffering, including the misrepresentation of the Company's financial statements, thus causing the Company to violate the federal securities laws and subjecting the Company to shareholder suits;

(d) they subjected the Company to a federal grand jury investigation of former and current Company executives for receiving payments from ADM to avoid taxes or for other improper and/or illegal purposes; and

(e) they subjected ADM to adverse publicity and damage to goodwill, which has greatly increased ADM's costs to raise capital and impaired its earnings.

75. The Director Defendants' wrongful conduct is a result of, among other things, their failure to maintain a system of internal controls adequate to insure the Company's compliance with the federal antitrust and securities laws. The Director Defendants' conduct has and will continue to cause considerable damage to ADM.

76. All of the Director Defendants, singly and in concert, engaged in the wrongful conduct in the intentional breach and/or reckless disregard of their fiduciary duties to the Company and its shareholders and conspired to, and did, abuse the control vested in them by virtue of their high-level positions in the Company.

77. ADM and its shareholders have been injured by reason of the Director Defendants' intentional breach and/or reckless disregard of their fiduciary duties to the Company. Plaintiffs, as shareholders and representatives of ADM, seek damages and other relief for the Company.

COUNT II

DERIVATIVE CLAIM AGAINST ALL DEFENDANTS FOR NEGLIGENT BREACH OF FIDUCIARY DUTIES

78. Except to the extent plaintiffs allege intentional or reckless misconduct by any defendant, plaintiffs incorporate by reference and reallege paragraphs 1 through 70 above as though set forth fully herein.

79. The Director Defendants engaged in the aforesaid conduct without exercising the reasonable and ordinary care owed to the Company by its directors, officers, managing agents and employees.

80. ADM and its shareholders have been injured by reason of the Director Defendants' negligent breaches of their fiduciary duties. Plaintiffs, as shareholders and representatives of ADM, seek damages and other relief for the Company.

COUNT III

DERIVATIVE CLAIM AGAINST THE DIRECTOR DEFENDANTS FOR ABUSE OF CONTROL

81. Plaintiffs incorporate by reference paragraphs 1 through 70 above as though set forth fully herein.

82. The Director Defendants' conduct constituted an abuse of their control of and influence over ADM for which they are legally responsible.

83. By reason of the foregoing, ADM has been damaged.

COUNT IV

DERIVATIVE CLAIM AGAINST THE DIRECTOR DEFENDANTS FOR GROSS MISMANAGEMENT

84. Plaintiffs incorporate by reference paragraphs 1 through 70 above as if fully set forth herein.

85. As detailed more fully herein, the Director Defendants had a duty to ADM and its stockholders to prudently supervise, manage and control ADM's operations.

86. These defendants, either directly or through aiding and abetting, abandoned and abdicated their responsibilities and duties to prudently manage the assets of ADM in a manner consistent with the operations of a publicly held corporation.

87. By acting as alleged herein, the Director Defendants breached their duties of due care and diligence in the management and administration of ADM's affairs and in the use and preservation of ADM's assets.

88. As a proximate result thereof, ADM has been damaged.

PRAYER FOR RELIEF

WHEREFORE, plaintiffs demand judgment on behalf of ADM as follows:

A. Against each defendant for restitution and/or damages in favor of plaintiffs, on behalf of ADM and its public stockholders, and awarding punitive and exemplary damages as appropriate, plus pre-judgment interest;

B Extraordinary equitable and/or injunctive relief as permitted by law, equity and state statutory provisions sued hereunder;

C. Awarding plaintiffs the costs and disbursements of this action, including reasonable attorneys', and experts' fees; and

D. Awarding such other relief as the Court may deem just and proper.

Plaintiffs hereby demand a trial by jury.

DATED: May 17, 1996

By: /s/ Terry Rose Saunders
One of the Attorneys
for Plaintiffs

[Counsel Listing Omitted]

[Verifications Omitted in Printing]

[Filed Jun. 7, 1996]

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS

[Caption Omitted in Printing]

DEFENDANTS' MOTION TO DISMISS THE CONSOLIDATED AND AMENDED DERIVATIVE COMPLAINT FOR FAILURE TO MAKE DEMAND AND FAILURE TO STATE A CLAIM

Defendants move the Court to enter an order dismissing plaintiffs' Consolidated Amended Derivative Complaint pursuant to Fed. R. Civ. P. 23.1.

1. The present action was instituted on or about July 13, 1995, in the United States District Court for the Northern District of Illinois. A notice of intent to file a "Proposed Consolidated and Amended Derivative Complaint" was filed in the Northern District of Illinois on Sept. 29, 1995.

2. This action was transferred to this Court on or about November 16, 1996.

3. Defendants filed a motion to dismiss plaintiffs' original consolidated complaint on December 27, 1995.

4. At the hearing on defendants' motion to dismiss on April 26, 1996, the Court dimissed plaintiffs' action for failure to file a verified complaint, giving plaintiffs leave to refile.

5. Plaintiffs filed their Consolidated and Amended Derivative Complaint ("Amended Complaint" or "Amended Compl." on May 17, 1996. In the Amended Complaint, plaintiffs allege that members of the board of directors

("the Individual Defendants") of nominal defendant Archer Daniels Midland Co. ("ADM") breached their fiduciary duty to shareholders by participating in or recklessly disregarding antitrust violations in three product areas (lysine, high fructose corn syrup, and citric acid). Amended Compl. ¶¶ 40-69. Plaintiffs also allege that the Individual Defendants authorized or approved illegal payments to ADM executives. *Id.* ¶¶ 70, 73.

6. Plaintiffs request the following relief: (i) damages on behalf of "ADM and its public stockholders" against the Individual Defendants; (ii) equitable and injunctive relief; and (iii) costs and attorneys' fees. *Id.*

7. Plaintiffs' Amended Complaint must be dismissed because plaintiffs failed to make a demand on the board of directors pursuant to Fed. R. Civ. P. 23.1 before filing this action.

8. In addition, plaintiffs have failed to show that demand was excused on grounds that it would be futile. Plaintiffs have failed to allege particularized facts that would raise a reasonable doubt that a majority of ADM's board was incapable of impartially considering a demand due to self-interest or lack of independence.

9. Defendants request oral argument to present fully the issue of why plaintiffs were required to make a pre-suit demand on the board of directors, and why their failure to do so requires dismissal.

WHEREFORE, the defendants pray that this Court dismiss plaintiffs' Consolidated and Amended Derivative Complaint for failure to comply with the demand requirement set forth in Fed. R. Civ P. 23.1.

[Counsel Listing Omitted]

DATED: June 7, 1996

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

[Caption Omitted in Printing]

SUPPLEMENT TO CONSOLIDATED AND AMENDED DERIVATIVE COMPLAINT

Plaintiffs hereby supplement their Consolidated and Amended Derivative Complaint as follows:

1. The following Paragraph 5A is inserted immediately after Paragraph 5:

5A. On October 15, 1996, ADM entered into a "Plea Agreement" with the United States Department of Justice in which ADM admitted to violating Section 1 of the Sherman Act, 15 U.S.C. § 1 and agreed, among other things, to pay a $100 million criminal fine. In addition to agreeing to pay $25 million to settle the lysine civil antitrust case, on September 27, 1996 ADM announce that it has agreed to pay $35 million to settle the citric acid civil antitrust case and to pay $30 million to settle a class action brought by ADM stock purchasers alleging federal securities law violations.

2. The following paragraphs 69A and 69B are inserted immediately after paragraph 69:

69A. On October 15, 1996, ADM entered into a "Plea Agreement" with the Department of Justice in which ADM agreed to plead guilty and pay a $100 million criminal fine—the largest criminal antitrust fine in U.S. history—for fix-

ing prices in the lysine market from June, 1992 through June 27, 1995 and for fixing prices in the citric acid market from January, 1993 through June 27, 1995. Pursuant to the guilty plea, ADM agreed to cooperate with the United States in current federal investigations of: (i) any antitrust schemes involving ADM's BioProducts Division, ADM's Animal Health and Nutrition Division, ADM's Food Additives Division or ADM's Sweetener Group; (ii) the acquisition by ADM of certain technology which is the subject of federal investigations in the Central District of Illinois and the Southern District of Alabama; and (iii) any investigation or proceedings arising from such investigations to which the U.S. is a party. ADM also agreed in its Plea Agreement to use its best efforts to secure the cooperation of any current director, officer or employee of ADM (other than Michael D. Andreas and Terrance S. Wilson), including making such persons and their documents available in the U.S., at ADM's expense, for service of process, interviews (except for defendants Dwayne Andreas and James Randall) relating to a pending indictment or information, grand jury testimony and trial testimony. In return, the U.S. agreed, among other things, not to bring criminal charges against any current director, officer or employee of ADM (other than Michael D. Andreas and Terrance S. Wilson) for any act or offense committed in furtherance of, or in connection with, the matters covered in the investigations referred to above.

69B. On September 27, 1996, ADM announced that it had agreed to pay $35 million to settle the citric acid civil antitrust case and to pay $30

million to settle a class action brought by ADM stock purchasers alleging violations of the federal securities laws. Both settlements are subject to court approval. These settlements are also to be paid directly by the Company and not by any insurance. In connection with the fines and settlements, ADM announced a $174 million charge to earnings for the quarter ended September 30, 1996.

[Counsel Listing Omitted]

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

[Caption Omitted in Printing]

AMENDMENT AND SUPPLEMENT TO CONSOLIDATED AND AMENDED DERIVATIVE COMPLAINT

Plaintiffs, by their attorneys, amend and supplement their Consolidated and Amended Derivative Complaint, as previously supplemented, to allege a new Count V against all Director Defendants except Howard G. Buffett relating to the acts and transactions previously alleged, as follows:

ADDITIONAL FACTS

The following Paragraph 69C is inserted immediately after Paragraph 69B:

69C. On December 3, 1996, M.D. Andreas, Terrance S. Wilson, former ADM Group Vice President and President of ADM's Corn Processing Division, and Mark E. Whitacre, former ADM Corporate Vice President and President of ADM's BioProducts Division, were indicted for conspiracy to fix prices and allocate sales volumes of lysine. The indictment lists eleven meetings between June, 1992 and June, 1995, and refers to numerous additional telephone conversations and other discussions between defendants and co-conspirators at which the prices and volumes of sales of lysine sold worldwide were discussed

and agreed to, and charges the defendants and co-conspirators with having taken steps to implement, monitor and police the unlawful price-fixing agreements.

COUNT V

DERIVATIVE CLAIM AGAINST ALL DIRECTOR DEFENDANTS EXCEPT HOWARD G. BUFFETT FOR BREACH OF FIDUCIARY DUTIES

88. Plaintiffs reallege and incorporate by reference paragraphs 1 through 70 as though fully set forth herein.

89. The Director Defendants are fiduciaries of ADM and all of its public shareholders and owe to them the duty to conduct the business of the Company loyally, faithfully, carefully, diligently and prudently. This Count is based upon the acts of the Director Defedants, other than defendant Buffett, in violation of Delaware common law, which acts constitute a breach of these defendants' fiduciary duty of loyalty, involve knowing or intentional misconduct, or were not in good faith.

90. The Director Defendants owed ADM and its stockholders the duty to investigate promptly charges of criminal conduct by ADM executives, evaluate objectively the evidence against Company officials and act to minimize ADM's exposure to criminal penalties that could result from ADM's antitrust violations. Faced with substantial evidence of high-level wrongdoing—particularly FBI videotapes of price-fixing meetings attended by defendant M.D. Andreas and Terrance S. Wilson, then ADM Group Vice President and President of ADM's Corn Processing Division—they had the duty to take all necessary steps to demonstrate that the Company intended to remedy, prevent reoccurence of and seek redress for any wrongdoing on the part of company officials.

91. The Director Defendants named in this Count, in their roles as executives and directors of the Company, participated in the acts of mismanagement alleged herein, or acted in reckless disregard of the facts known to them. They breached their fiduciary duties of care and loyalty by failing to conduct a thorough and objective investigation of wrongdoing and, in the face of the substantial evidence the government had accumulated, by refusing to cooperate with or assist the Department of Justice in connection with the government's investigation of the Company executives—particularly M.D. Andreas and Terrance S. Wilson. The Director Defendants' conduct was designed to, and did, serve the interests of the Andreas family at the expense of ADM and its shareholders. The Defendants' improper behavior includes, but is not limited to, the following:

(a) Upon learning of the government's investigation, ADM executives determined to withhold information from the public. The Director Defendants went along with this policy. Indeed, former director and officer Howard G. Buffett resigned his positions one week after the June 27, 1995 FBI subpoenas became public "because he was troubled by the [government's] investigation and the way the Company was handling it," and because he had "lost confidence" in whether ADM executives were telling him the truth. (*See* paragraph 66, above.)

(b) ADM's Board of Directors delegated responsibility for ADM's response to the government's investigation to a Special Committee of the Board composed of friends and associates of D. Andreas. (*See* paragraphs 31-34, above.) This Committee was more concerned about protecting the Andreas family's interests than in ensuring that the thorough and impartial investigation necessary to protect the interests of the Company and its shareholders was conducted

immediately. Members of the Committee delayed and failed to take any steps against ADM officers accused of participating in the conspiracy and, instead, publicly criticized the FBI. For example, in October 1995, Special Committee member F. Ross Johnson delivered a widely publicized speech at Emory University, in which he stated:

> It turned out . . . that the FBI, who have got some good scumbags in there too—its almost a criminal mentality [he snickers]—he came in and got the goods on this guy [Whitacre] in one way or another, and for immunity [in Jan., 1993, he] signed this great long agreement . . . They [FBI] like to extort. Their technique is to get the gun on somebody and then put the pressure on. And then that puts the pressure on somebody else.

(*Wall Street Journal*, October 12, 1995; *Fortune*, October 30, 1995.)

(c) The Director Defendants' immediate reaction to allegations of price fixing was to investigate Whitacre, the President of the BioProducts Division who had become an FBI informant. In order to discredit the government's antitrust investigation, ADM moved quickly to build a case against Whitacre for embezzling funds (which Whitacre claimed to have received pursuant to a Company income tax evasion scheme) and terminated Whitacre and two other executives. (*Wall Street Journal*, August 21, 1995, September 25, 1995 and March 27, 1996; *New York Times*, September 27, 1995.)

(d) At the same time, however, the Director Defendants took no action against M.D. Andreas (only son and expected successor of D.O. Andreas) and Terrance S. Wilson, who were permitted to remain in their positions, and given raises, although de-

fendants knew that they were targets of a federal grand jury investigation and that indictments were being considered. After ADM entered into a plea agreement, ADM announced that Wilson had taken "early retirement", and M.D. Andreas had taken "temporary administrative leave." M.D. Andreas and Wilson, as well as Whitacre, were indicted on December 3, 1996 for their participation in the lysine price-fixing conspiracy.

(e) As evidence of wrongdoing continued to mount and after the outside directors had been briefed on the contents of the FBI's incriminating videotapes, they continued their "united front" in fighting the government. (*Wall Street Journal,* March 27, 1996.)

(f) Shortly after the government's investigation became public, ADM's co-conspirators in the lysine price-fixing scheme recognized that the government had "accumulated substantial evidence" and began quietly talking to the government about possible cooperation. ADM, however, in the words of one co-conspirator," was railing regularly in the press against the government's investigation in general and the manner in which the informant was used in particular." (*See* Transcript of October 18, 1996 proceedings in *United States v. Ajinomoto Co., Inc.* at 9.)

(g) In response to the January, 1996 report by ADM's corporate governance committee, the Director Defendants reduced ADM's board from seventeen to twelve members and nominated new directors. However, rather than nominating a truly independent Board to ensure that appropriate steps were taken to remedy wrongdoing and restore public confidence, the Director Defendants continue to serve on the Board and have failed to add strong independent directors to counterbalance the influence of D.O. Andreas. Indeed, one of the new directors is Ms. Mollie

Hale Carter, daughter of outgoing director H.D. Hale. Not surprisingly, ADM's institutional shareholders maintain that the board still lacks independence, and, at the October 17, 1996 annual meeting, 42% of the stock was voted in favor of a resolution to compel ADM to form a board consisting of a majority of directors meeting a more stringent definition of independence than ADM's current definition.

91. The failure of the Director Defendants to react appropriately to the charges of wrongdoing is the result of the dominance that D.O. Andreas exercises over the Board. ADM's board continues to be criticized for its lack of independence and only recently was ranked as the worst board in corporate America by *Business Week* in an evaluation reflecting opinions of shareholders and corporate governance experts. ADM's institutional investors believe that ADM's directors, "co-opted by family ties, business links, and longstanding friendships, put shareholder interests behind those of [Dwayne] Andreas." (*Business Week,* "The Best & Worst Boards", November 25, 1996, at 82.)

92. The continued refusal of the Director Defendants to take steps necessary and appropriate to limit ADM's exposure to severe criminal fines and penalties was further evidenced by the Company's September 1996 personal mailing to its shareholders of copies of *Washington Times* articles that called the government's case a "frame-up" designed to meet the Justice Department's quota for white-collar crimes and "fabricated" and accused the U.S. Government of "teaming up" with ADM's more cooperative foreign competitors whose testimony was "obviously tainted." According to Columbia Law School professor John C. Coffee, Jr., "One impact of this kind of conduct is that it will injure the shareholders by possibly precluding the company from claiming acceptance of responsibility." (*New York Times,* September 13, 1996.)

93. The injury that the conduct of the Director Defendants caused ADM and its shareholders is evidenced by the severity of ADM's fines as compared to treatment recommended for ADM's co-conspirators Ajinomoto Co., Inc. and Sewon America, Inc. During the October 18, 1996 hearings on these co-conspirators' plea and sentencing agreements, the government stressed that the co-conspirators had cooperated early and had assisted the government in its investigation.

> (a) With respect to Sewon America, Inc., the government agreed to file a motion to ask the court to depart from Section 8C2.7 of the federal sentencing guidelines "because of the defendant's substantial assistance to the investigation of other individuals and corporations for violation of federal criminal laws." (Transcript of October 18, 1996 proceedings in *United States v. Sewon America, Inc.*, at 9.)
>
> (b) With respect to Ajinomoto Co., Inc., the government stated, "Ajinomoto did cooperate with the government early in this investigation, and the value of their cooperation has been acknowledged publicly . . . The value of their cooperation we believe was taken into account fully in the sentencing agreement. We are going to be recommending a sentence of a $10 million fine." (Transcript of October 18, 1996 proceedings in *United States v. Ajinomoto Co., Inc.*, at 4). The Government further emphasized that Ajinomoto's "cooperation was timely, early and valuable." (*Id.* at 21.)

95. In contrast to the cooperating defendants for whom the government recommended a lesser fine, ADM, was required to pay a fine of $100 million—the largest antitrust penalty ever—in return for the government's acceptance of a guilty plea. This harm was caused by the Director Defendants' refusal to cause ADM to cooperate with the government or to demonstrate a willingness to take remedial steps against M.D. Andreas and Terrance S. Wilson, who were known to be targets of a federal grand jury investigation.

96. The Director Defendants, singly and in concert, engaged in the wrongful conduct in breach of their fiduciary duties to the Company and its shareholders; and conspired to, and did, abuse the control vested in them by virtue of their high-level positions in the Company.

97. ADM and its shareholders have been injured by reason of the Director Defendants' breaches of their fiduciary duties to the Company, as alleged above. Plaintiffs, as shareholders and representatives of ADM, seek damages and other relief for the Company.

WHEREFORE, plaintiffs demand judgment on behalf of ADM as follows:

A. Against each defendant for restitution and/or damages in favor of plaintiffs, on behalf of ADM and its public stockholders, and awarding punitive and exemplary damages as appropriate, plus pre-judgment interest;

B. Extraordinary equitable and/or injunctive relief as permitted by law, equity and state statutory provisions sued hereunder;

C. Awarding plaintiffs the costs and disbursements of this action, including reasonable attorneys', and experts' fees; and

D. Awarding such other relief as the Court may deem just and proper.

DATED: December 6, 1996

[Counsel Listing Omitted]

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

[Caption Omitted in Printing]

AGREED MOTION FOR AN ORDER PRELIMINARILY APPROVING SETTLEMENT, SCHEDULING A FINAL SETTLEMENT HEARING AND DIRECTING THAT NOTICE BE GIVEN TO THE SHAREHOLDERS OF ARCHER DANIELS MIDLAND COMPANY

Plaintiffs, by their counsel, move, pursuant to Fed. R. Civ. P. 23.1, for an order (a) preliminarily approving the settlement of the derivative claims asserted in this action; (b) scheduling a hearing to consider final approval of the settlement and Plaintiffs' counsel's request for an award of fees and expenses; and (c) authorizing the form and manner of notice to be given to Archer Daniels Midland Company's shareholders. In support of this motion, Plaintiffs state as follows:

1. This action was commenced in the United States District Court for the Northern District of Illinois and the Circuit Court of Cook County, Illinois in July 1995. Subsequently, the cases were transferred to and consolidated in this Court.

2. Plaintiffs' counsel and counsel for the Defendants and the Company have reached a proposed settlement with the Company and the Defendants that includes implementation of corporate governance measures and the payment on behalf of the Defendants of $8 million, a significant portion of which will be used by the Company in implementing the corporate governance measures. A copy of the Stipulation of Settlement is attached as Exhibit A.

3. The Settlement was achieved following Plaintiffs' counsel's substantial fact investigation, consultation with independent experts and certain of the Company's major institutional investors, and arm's length negotiations between Plaintiffs' counsel and counsel for the Company and the Defendants.

4. The settlement will confer substantial benefits on the Company and its shareholders and is within the range of possible approval by the Court.

WHEREFORE, Plaintiffs request that the Court enter an order:

(a) Granting preliminary approval of the settlement;

(b) Approving the proposed notice of settlement attached hereto as Exhibit B; directing that notice of the settlement in the form attached as Exhibit "B-1" be mailed to Class members; and directing that publication notice in the form attached as Exhibit "B-2" be published in the national edition of *The Wall Street Journal*.

(c) Approving the timetable for giving notice to the shareholders of Archer Daniels Midland Company and holding a hearing to consider approval of the settlement, as set forth in the Order Preliminarily Approving Settlement and Providing for Notice.

Respectfully submitted,

[Counsel Listing Omitted]

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

[Caption Omitted in Printing]

STIPULATION OF SETTLEMENT

This Stipulation of Settlement (the "Stipulation"), dated as of May 29, 1997, is made and entered into by and among (i) the Plaintiffs in the Illinois Action and the Delaware Action on behalf of themselves, the shareholders of Archer Daniels Midland Company ("ADM" or the "Company") and derivatively on behalf of the nominal defendant ADM, (ii) the Director Defendants, and (iii) nominal defendant ADM (collectively the "Parties"), as those terms are defined herein, by and through their counsel of record in the Actions. The Stipulation is intended by the Parties to fully, finally and forever resolve, discharge and settle the Settled Claims (as defined herein), upon and subject to the terms and conditions hereof.

I. THE LITIGATION

This litigation was commenced in July 1995, with the filing of shareholder derivative actions in the United States District Court for the Northern District of Illinois, the Circuit Court of Cook County, Illinois and the Delaware Court of Chancery (the "Delaware Court"). The actions filed in Illinois were transferred to the United States District Court for the Central District of Illinois (the "District Court"), and Plaintiffs filed a Consolidated and Amended Derivative Complaint, entitled *Paul Felzen, Trustee of Louise Laskin Trust - 1991 and Sandra Esner, Plaintiffs, v. Dwayne O. Andreas, et al., Defendants, and Archer Daniel Midland Company, Nominal Defendant,* Case No. 2279 (the "Illinois Action"). In November

1996, the Plaintiffs in the action brought in the Delaware Court filed an amended and consolidated complaint entitled *In Re Archer Daniels Midland Company Derivative Litigation,* Consolidated No. 14403 (the "Delaware Action"), to add allegations relating to events that occurred during 1996. Both the Illinois Action and the Delaware Action (the "Actions") named as defendants Dwayne O. Andreas, Ralph Bruce, John H. Daniels, Howard G. Buffett, Lowell W. Andreas, James R. Randall, Michael D. Andreas, H.D. Hale, O. Glenn Webb, Martin Andreas, Margaretta Rockefeller, F. Ross Johnson, Ray A. Goldberg, John K. Vanier, Shreve M. Archer, Jr., M. Brian Mulroney, and Robert S. Strauss, and the Delaware Action also named Gaylord O. Coan as a defendant (the "Director Defendants"). The Actions alleged, among other things, that the Director Defendants breached their fiduciary duties owed to the Company and its stockholders by participating in improper conduct or failing to properly supervise the activities of certain employees of the Company who had engaged in improper conduct, including violations of federal antitrust laws and federal securities laws. The shareholders' derivative claims are sometimes referred to collectively as the "litigation".

Plaintiffs in the Illinois Action filed a Supplement to Consolidated and Amended Derivative Complaint on November 4, 1996 and an Amendment and Supplement to Consolidated and Amended Derivative Complaint on December 6, 1996 to add allegations relating to events that occurred after May 17, 1996.

II. PRETRIAL PROCEEDINGS AND DISCOVERY IN THE LITIGATION

A. *Defendants' Actions*

The Director Defendants and the Company have filed motions to dismiss the Actions. In their motions to dismiss, the Director Defendants and the Company argued that Plaintiffs failed to make a demand upon the directors

of ADM as required by Delaware law before bringing their action, that Plaintiffs failed to state a claim for relief against the Director Defendants and that, under Article Fourteenth of ADM's Certificate of Incorporation, defendants are not liable for any of the breaches of duty alleged in the Actions. Plaintiffs opposed the motions.

The District Court has not ruled on the motion to dismiss and has adjourned oral argument on the motion, pending a hearing by the Court at which this Stipulation and the settlement are to be presented. Similarly, the Delaware Court has not ruled on defendants' motion to dismiss. The Parties to the Delaware Action agree to advise the Delaware Court of the proposed settlement as soon as practicable and to hold in abeyance all proceedings other than those set forth in the MOU or Stipulation that are required to obtain Final Court Approval.

After the announcement of the federal government's investigation into the charges that ADM had violated the antitrust laws and the filing of these Actions and class action lawuits for violation of the federal securities and antitrust laws, ADM's Board of Directors appointed a Special Committee consisting of outside directors to "direct the Company's response to matters related to the government investigation of the high fructose corn syrup, citric acid and lysine industries and certain related civil suits." The Special Committee retained counsel to assist it.

After the Illinois Action and the Delaware Action were filed and the allegations reviewed, the Company undertook certain actions in the areas of corporate governance, employee conduct, compliance, and succession.

On October 21, 1995, ADM's Board of Directors created the Corporate Governance Committee, consisting of outside directors to examine the Board's size, director qualifications, independence from management, ethics, compensation and other issues. The Corporate Governance Committee reported its recommendations to the

Board on January 15, 1996, including recommendations establishing requirements for an independent Board. In the Spring of 1996, the Company announced that certain of its directors, including Michael D. Andreas, would not stand for re-election. Three new directors were elected to the Board at the annual meeting of shareholders in October, 1996. In April, 1997, the Company announced that Dwayne Andreas had retired from his position as CEO of the Company and that G. Allen Andreas, Jr. would become the CEO and a member of the Board. In addition, the Company announced the election of Ambassador Andrew Young to the Board and the retirement of Lowell Andreas from the Board.

B. *Discovery, Investigation And Research Conducted By Plaintiffs*

Counsel for Plaintiffs have conducted an extensive investigation during the prosecution of the Actions, including consulting with experts in the areas of corporate governance and economics, and with the Company's largest institutional investors, and reviewed and analyzed treatises, articles, and authoritative reports on corporate governance issues. In addition, Plaintiffs' Counsel reviewed and analyzed thousands of pages of documents produced by defendants, reviewed and analyzed the Company's public filings and press releases, and thoroughly analyzed and evaluated the facts supporting Plaintiffs' claims.

C. *The Settlement Negotiations*

Beginning in November, 1996, Co-Lead counsel for Plaintiffs in the Illinois Action and counsel for the defendants met and reached an agreement in principle under which the Company would implement certain procedures and measures for corporate governance. Subsequently, in order to obtain the global resolution of the Actions, there were further negotiations between Co-Lead Counsel for Plaintiffs in the Delaware Action and defend-

ants leading to additional provisions for corporate governance measures. These vigorous, arms-length negotiations culminated in the execution of the Memorandum of Understanding on May 29, 1997, including the terms reflected in Exhibit A to the Memorandum of Understanding and to this Stipulation.

III. DEFENDANTS' STATEMENT AND DENIALS OF WRONGDOING AND LIABILITY

Each of the Director Defendants has denied and continues to deny each and all of the claims and contentions alleged by Plaintiffs in the Litigation. Each of the Director Defendants expressly has denied and continues to deny all charges of wrongdoing or liability against him or her arising out of the conduct, statements, acts or omissions alleged, or that could have been alleged, in the Litigation. Each of the Director Defendants further asserts that at all material times, he or she acted in good faith and in a manner he or she reasonably believed to be in the best interest of ADM and its shareholders.

Despite their assertions, the Director Defendants have concluded that the further conduct of the Litigation would be protracted and expensive, and that it is desirable that the Litigation be fully and finally settled in the manner and upon the terms and conditions set forth in this Stipulation in order to limit further expense, inconvenience and distraction, to dispose of burdensome and protracted litigation, and to permit the operation of ADM's business without further expensive litigation and the distraction and diversion of ADM's executive personnel with respect to matters in issue in the Litigation.

Moreover, the Director Defendants recognize that the procedures and measures that are set forth in Exhibit A, and which the Company will implement as part of the Settlement, will provide substantial benefits and protections to the Company and its shareholders.

IV. CLAIMS OF THE PLAINTIFFS AND BENEFITS OF SETTLEMENT

The Plaintiffs believe that the claims asserted in the Litigation have merit. However, counsel for the Plaintiffs recognize the expense and length of continued proceedings necessary to prosecute the Litigation against the Director Defendants through trial and through appeals. Counsel for the Plaintiffs have taken into account the uncertain outcome and the risk of any litigation, especially complex derivative actions such as this Litigation, as well as the difficulties and delays inherent in such litigation. Counsel for the Plaintiffs have taken into account the strengths and uncertainties and the possible defenses to the claims asserted in the Litigation, including the defenses asserted by defendants in their motions to dismiss the Litigation, and the substantial benefits of corporate governance procedures and measures contained in the Settlement, as well as the benefit from the termination of the Litigation.

In light of the foregoing, counsel for the Plaintiffs believe that the settlement set forth in the Stipulation confers substantial benefits upon ADM and its shareholders and have determined that the settlement set forth in the Stipulation is in the best interests of ADM and its shareholders.

V. TERMS OF STIPULATION AND AGREEMENT OF SETTLEMENT

NOW, THEREFORE, IT IS HEREBY STIPULATED AND AGREED by and between the Plaintiffs (for themselves, the shareholders of ADM and derivatively on behalf of ADM), nominal defendant ADM, and each of the defendants, by and through their respective counsel or attorneys of record that, subject to the approval of the District Court, the Litigation and all Settled Claims shall be finally and fully compromised, settled and released, and the Litigation shall be dismissed with prej-

udice, upon and subject to the terms and conditions of the Stipulation, as follows:

A. *Definitions*

(a) "Actions" as utilized herein shall mean collectively the Delaware Action (as defined herein) and the Illinois Action (as defined herein).

(b) "Andreas" as utilized herein shall mean Michael D. Andreas, his heirs, executors, administrators, successors, assigns, agents, employees, attorneys, representatives, and any person or entity claiming by or through him.

(c) "Company" as utilized herein shall mean Archer Daniels Midland Company, a Delaware corporation, and its directors, officers, agents, employees, representatives, attorneys, insurers, successors, assigns, parents, subidiaries, partners, and affiliates, except said term shall not include Excluded Persons (as defined herein), Andreas (as defined herein), or Wilson (as defined herein).

(d) "Co-Lead Counsel for Plaintiffs", as utilized herein shall mean, in the Illinois Action (as defined herein) Robert M. Roseman, Spector & Roseman, P.C. and Terry Rose Saunders, Law Offices of Terry Rose Saunders; and in the Delaware Action (as defined herein) Susan Salvetti of Zwerling, Schacter & Zwerling, LLP; Robert I. Harwood of Wechsler Harwood Halebian & Feffer LLP, and Stanley Bernstein of Bernstein Liebhard & Lifshitz.

(e) "Delaware Action" as utilized herein shall mean those actions or litigation pending currently before the Delaware Court (as defined herein), following consolidation, as *In Re Archer Daniels Midland Company Derivative Litigation*, Consolidated No. 14403, and any appeals (interlocutory or otherwise) taken from those actions.

(f) "Delaware Court" as utilized herein shall mean the Delaware Court of Chancery wherein the Delaware Action (as defined herein) is currently pending, and any

court of review to which an appeal has been taken from the Delaware Action (as defined herein).

(g) "Director Defendants" as utilized herein shall mean the Individual Defendants (as defined herein) and Andreas (as defined herein).

(h) "District Court" as utilized herein shall mean the United States District Court for the Central District of Illinois wherein the Illinois Action (as defined herein) is currently pending.

(i) "Effective Date" as utilized herein shall mean the date upon which Final Court Approval occurs.

(j) "Escrow Account" as utilized herein shall mean a certain interest-bearing account with Hickory Point Bank and Trust in Forsyth, Illinois into which the Settlement Proceeds (as defined herein) have been deposited which account is subject to certain restrictions in order to effectuate its purpose as described herein. The Settlement Proceeds have been and shall continue to be invested in United States Treasury Securities having maturities no greater than seven (7) days, or their equivalent.

(k) "Excluded Persons," as utilized herein shall mean Mark E. Whitacre, Reinhard Richter, Sidney Hulse, and Marty Allison.

(l) "Final Court Approval" as utilized herein shall mean the acceptance by the District Court (as defined herein) of the Stipulation of Settlement (as defined herein), said District Court's determination that the settlement of the Actions is fair, reasonable, and adequate, said District Court's approval of said settlement, including dismissal with prejudice of the Illinois Action (as defined herein) against the Company (as defined herein) and the Individual Defendants (as defined herein), without the award of their costs or expenses, the dismissal with prejudice of the Delaware Action (as defined here-

in) against the Company (as defined herein) and the Individual Defendants (as defined herein) without the award of their costs or expenses, and the dismissal without prejudice of claims in the Actions (as defined herein) directed against Andreas (as defined herein), which claims shall become the sole property of the Company, and the affirmance on appeal of said dismissals without further appeal or by lapse of time no appeal or further appeal is available.

(m) "Illinois Action" as utilized herein shall mean that action or litigation pending currently before the District Court (as defined herein), following consolidation, as *Paul Felzen, Trustee of Louise Laskin Trust—1991 and Sandra Esner, Plaintiffs v. Dwayne O. Andreas, et al., Defendants and Archer Daniels Midland Company, Nominal Defendant*, Cause No. 95-2279.

(n) "Individual Defendants" as utilized herein shall mean all current and former members of the Board of Directors of the Company (as defined herein), identified or referred to in the Actions (as defined herein) except Andreas (as defined herein).

(o) "Judgment" as utilized herein shall mean the final Judgment and Order of Dismissal With Prejudice to be rendered by the District Court.

(p) "MOU" as utilized herein shall mean the Memorandum of Understanding entered into among the Parties as of May 29, 1997.

(q) "Net Settlement Proceeds" as utilized herein shall mean the Settlement Proceeds, less: (i) attorneys fees and expenses, (ii) costs of notice, and (iii) any other fees and expenses as may be authorized by the Court.

(r) "Notice" as utilized herein shall mean the Notice of Hearing on Proposed Settlement of Derivative Action, substantially in the form annexed hereto as Exhibit B-1.

(s) "Parties" as utilized herein shall mean Plaintiffs, Director Defendants and ADM in this Litigation.

(t) "Plaintiffs' Settlement Demands" as utilized herein shall mean those claims and demands contained within pleadings of the Plaintiffs in the Actions (as defined herein) together with certain alternative remedial measures and procedures, which, on the basis of investigation and analysis by legal counsel for the Plaintiffs, said legal counsel believed were sufficient to form a basis for exploration of a possible settlement of the Actions (as defined herein).

(u) "Preliminary Approval Order" as utilized herein means the Order Preliminarily Approving Settlement and Providing for Notice, substantially in the form attached hereto as Exhibit B.

(v) "Settled Claims" as utilized herein shall mean any and all causes of action, suits, demands, claims, matters and issues, whether known or unknown, which have been, could have been, or in the future might be asserted, advanced or alleged in any of the Actions (as defined herein) or in any court or arbitration proceeding (including, without limitation, any claims, actions or demands arising under any federal or state law relating to alleged fraud, breach of any duty, negligence, recklessness, violations of federal or state securities laws, violations of federal or state antitrust laws or otherwise) by or on behalf of the Company (as defined herein), by any shareholder of said Company derivatively on its behalf, or by any named Plaintiff in the Actions (as defined herein) on their own behalf or on behalf of any record or beneficial holder of the stock of the Company (as defined herein), whether individual, class, derivative, representative, legal, equitable, or any other type in any other capacity, which claims have arisen, could have arisen, arise now or hereafter arise out of, or relate in any manner to the allegations, transactions, matters or occurrences, representations, acts

or omissions, or any series thereof, involved, set forth, referred to, or related to any of the pleadings in the Actions (as defined herein) against the Company (as defined herein) and or any of the Individual Defendants (as defined herein), provided, however, that Settled Claims shall not include any claims which the Company may have against Andreas (as defined herein), Wilson (as defined herein), or the Excluded Persons (as defined herein), which claims shall be reversed to the Company in its sole discretion.

(w) "Settlement Proceeds" as utilized herein shall mean the sum of Eight Million Dollars (8,000,000) paid by or on behalf of the Director Defendants (as defined herein) to the Company (as defined herein) by placement thereof into the Escrow Account (as defined herein) within forty-eight (48) hours after execution of the MOU (as defined herein) by an authorized representative of the Company (as defined herein) which deposit thereof shall constitute the sole and exclusive liability of the Individual Defendants, and following said deposit, such liability will be terminated in its entirety except for payment of said Settlement Proceeds including interest earned thereon as set forth herein, subject to Section F, paragraph 2 of this Stipulation of Settlement. The Settlement Proceeds shall not be disbursed until Final Court Approval (as defined herein) and an order has been entered by the District Court directing disbursement consistent with this Stipulation of Settlement.

(x) "Stipulation of Settlement" or "Stipulation" as utilized herein shall mean this Stipulation of Settlement.

(y) "Wilson" as utilized herein shall mean Terrance B. Wilson, his heirs, executors, administrators, successors, assigns, agents, employees, attorneys representatives, and any person or entity claiming by or through him.

B. *The Settlement*

In consideration of the mutual covenants and agreements contained in this Stipulation, the Parties agree to the following:

1. Within sixty (60) days of Final Court Approval, the Company will implement the procedure set forth in Exhibit A to this Stipulation, which Exhibit is incorporated fully herein by reference.

2. In payment of the settlement set forth in this Stipulation, the Settlement Proceeds have been deposited in the Escrow Account on behalf of the Director Defendants pursuant to the terms of the MOU. Pending distribution pursuant to the terms of this Stipulation, the Settlement Proceeds will be held in the Escrow Account and remain invested in United States treasury securities having maturities no greater than seven (7) days, or their equivalent. The Settlement Proceeds shall not be disbursed until Final Court Approval and entry of an order by the District Court directing disbursement. The Settlement Proceeds shall be used to pay reasonable attorneys fees and expenses to legal counsel for the Plaintiffs as ordered by the District Court and reasonably and necessarily incurred costs and expenses associated with the provision of notice of any hearing scheduled by the Court in accordance with the Preliminary Approval Order.

3. Upon Final Court Approval, the Net Settlement Proceeds, and accrued interest thereon, shall be paid to the Company to pay expenses, costs, and legal fees incurred by the Audit Committee of the Board of Directors of the Company (the "Audit Committee"), at its discretion, for a period of at least three (3) years from the date of Final Court Approval, to satisfy its independent review responsibilities as set forth in Exhibit A, and for any training or educational efforts undertaken at the Audit Committee's direction.

4. Except as may be provided expressly herein and upon Final Court Approval, neither the Company nor the Director Defendants shall bear any other expense, damage, cost, liability, or fee in conjunction with any settlement or resolution of the Actions. No Director Defendant shall have any further liability in relation to the Actions whatsoever subject to Section F, paragraph 2 of this Stipulation.

5. All claims that the Company has against the Excluded Persons, and which the Company may have against Andreas and Wilson, are reserved to the Company and are not released by this Stipulation, nor are they Settled Claims.

C. *Attorneys' Fees and Costs*

Counsel for the Plaintiffs in the Actions may make application to the District Court for an award of attorney fees, expenses and costs. No application for an award of attorney fees, expenses, and/or costs shall be made in any other forum. The Company and the Director Defendants agree not to oppose an application(s) for an award of attorney fees, costs and expenses made to the District Court by Co-Lead Counsel for the Plaintiffs in the Illinois and Delaware Actions which does not exceed $3,920,000 of the Settlement Proceeds, plus interest. Any payment of an amount awarded by the District Court as fees, costs and expenses shall be made solely from the Settlement Proceeds, and shall not be made until Final Approval, and will be paid to Co-Lead Counsel for Plaintiffs in the Actions, as directed by the District Court, within three (3) business days after the District Court's order directing disbursement of the Settlement Proceeds.

D. *Preliminary Approval Order And Settlement Hearing*

1. Promptly after execution of the Stipulation, Co-Lead Counsel for Plaintiffs in the Illinois Action shall submit the Stipulation together with its Exhibits to the

District Court. The Parties in the Illinois Action shall jointly apply for entry of the Preliminary Approval Order, substantially in the form of Exhibit "B" hereto, requesting, *inter alia*, approval of the Settlement set forth in the Stipulation and approval for the mailing and publication of the Notice and Summary Notice to current shareholders of ADM which shall include the general terms of the Settlement set forth in the Stipulation, and the date of the Settlement Hearing. The Parties shall also request that, after notice is given, the District Court hold a hearing (the "Settlement Hearing") and approve the Settlement as set forth herein.

2. The Preliminary Approval Order shall specifically include provisions that, among other things, will:

a. Preliminarily approve the Stipulation and the Settlement set forth herein as being fair, reasonable and adequate to ADM and its shareholders;

b. Approve the form of Notice of Settlement ("Notice") (substantially in the form of Exhibit B-1 hereto) for mailing to current shareholders of ADM;

c. Approve a Summary Notice of the proposed settlement for publication (the "Summary Notice") (substantially in the form of Exhibit B-2 hereto);

d. Direct the Company to mail or cause to be mailed by first class mail the Notice to those current shareholders who can be identified through reasonable effort, on or before the date specified in the Preliminary Approval Order;

e. Request that nominees who currently hold ADM common stock send the Notice to all beneficial owners of such ADM common stock within ten (10) days after receipt of the Notice;

f. Direct the Company to cause the Summary Notice to be published in the national edition of *The Wall Street Journal* on or before the date specified in the Preliminary Approval Order;

g. Find that the notice given pursuant to subparagraphs (b)-(f), above, constitutes the best notice practicable under the circumstances, including individual notice to all current shareholders of ADM who can be identified upon reasonable effort, and constitutes valid, due and sufficient notice to all current shareholders of ADM, complying fully with the requirements of Rule 23.1 of the Federal Rules of Civil Procedure, the Constitution of the United States, and any other applicable law;

h. Schedule the Settlement Hearing to be held by the District Court to consider and determine whether the proposed Settlement as contained in the Stipulation should be approved as fair, reasonable and adequate to ADM and its shareholders and whether the Judgment approving the Settlement should be entered;

i. Provide that any objections to: (i) the proposed Settlement contained in the Stipulation or (ii) entry of the Judgment approving the Settlement, shall be heard and any papers submitted in support of said objections shall be considered by the District Court at the Settlement Hearing only if, on or before the date specified in the Preliminary Approval Order and Notice, shareholders of ADM making such objections shall file and serve notilce of their intention to appear and copies of any papers in support of their position (which shall set forth each objection and the basis therefor) as set forth in the Preliminary Approval Order and Notice;

j. Provide that, upon the Effective Date, all shareholders of ADM and ADM shall be barred from asserting any Settled Claims and each and all shareholders of ADM and ADM shall conclusively be deemed to have released any and all such Settled Claims and that all claims which the Company has against the Excluded Persons, or may have against Andreas and Wilson, are not Settled Claims and shall be reserved to the Company in its sole discretion; and

k. Provide that the Settlement Hearing may, from time to time and without further notice to shareholders of ADM, be continued or adjourned by order of the District Court.

3. Upon approval of the Settlement by the District Court, Co-Lead Counsel for Plaintiffs in the Delaware Action will take all steps necessary in the Delaware Court to obtain Final Court Approval as promptly as may be done.

E. *Releases*

1. Upon the Effective Date, each shareholder of ADM shall be deemed to have, and by operation of the Judgment shall have, fully, finally and forever released, relinquished and discharged all Settled Claims.

2. Upon the Effective Date, each of the Director Defendants and ADM shall be deemed to have, and by operation of the Judgment shall have, fully, finally and forever released, relinquished and discharged each and all shareholders of ADM and counsel to the plaintiffs, each only in their capacity as such, from all claims, arising out of, relating to or in connection with the institution, prosecution, assertion or resolution of the Litigation or the Settled Claims.

3. Upon the Effective Date, ADM shall be deemed to have, and by operation of the Judgment shall have, fully, finally and forever discharged all Settled Claims, with ADM reserving to itself any claims which it has against the Excluded Persons, or which ADM may have against Andreas or Wilson.

F. *Conditions Of Settlement Effect Of Disapproval, Cancellation Or Termination*

1. The Stipulation is subject to the following conditions:

a. The District Court enters the Preliminary Approval Order;

b. The District Court approves the Stipulation and enters the Judgment.

c. The Effective Date occurs.

2. If any of the conditions in Section F, Paragraph 1 does not occur, the Stipulation shall be rendered null and void, unless the Parties mutually agree in writing to proceed with the Stipulation. In the event of such non-occurrence, the Parties shall be restored to their respective positions in the Actions prior to the execution of the Stipulation, and the terms and provisions of the Stipulation shall have no further force and effect with respect to the Parties and shall not be used in the Litigation or in any other proceeding, for any purpose, and any Judgment or Order entered by the District Court in accordance with the terms of the Stipulation shall be treated as vacated.

G. *Miscellaneous Provisions*

1. The Parties (a) acknowledge that it is their intent to consummate this agreement, and (b) agree to cooperate to the extent necessary to effectuate and implement all terms and conditions of the Stipulation and to exercise their best efforts to accomplish the terms and conditions of the Stipulation.

2. Neither the Stipulation nor the Settlement, nor any act performed or document executed pursuant to or in furtherance of the Stipulation or the Settlement: (i) is or may be deemed to be or may be used as an admission of, or evidence of, the validity of any Settled Claim or of any wrongdoing or liability of the Director Defendants or the Company; or (ii) is or may be deemed to be or may be used as an admission of, or evidence of, any fault or omission of any of the Director Defendants or the Company, in any civil, criminal or administrative proceeding

in any court, administrative agency or other tribunal, other than in such proceedings as may be necessary to consummate or enforce the Stipulation, the Settlement or the Judgment, and provided that the Director Defendants or the Company may file the Stipulation and/or the Judgment in any action that may be brought against any of them in order to support a defense or counterclaim based on principles of *res judicata*, collateral estoppel, release, good faith settlement, judgment ban or reduction or any other theory of claim preclusion or issue preclusion or similar defense or counterclaim. The Director Defendants and the Company have denied and continue to deny each and all of the claims alleged in the Litigation.

3. The Parties and their counsel, and each of them, agree, to the extent permitted by law, that all agreements made and orders entered during the course of the Litgation relating to the confidentiality of information shall survive this Stipulation.

4. All Exhibits to the Stipulation are material and integral parts hereof and are fully incorporated herein by this reference.

5. The Stipulation may be amended or modified only by a written instrument signed by or on behalf of all Parties or their respective sucessors-in-interest.

6. The Stipulation and the Exhibits attached hereto constitute the entire agreement among the Parties hereto and no representations, warranties or inducements have been made to any party concerning the Stipulation or its Exhibits other than the representations, warranties and covenants contained and memorialized in such documents.

7. Each counsel or other person executing the Stipulation or any of its Exhibits on behalf of any party hereto hereby warrants that such person has the full authority to do so.

8. No Party hereto shall make, or permit to be made, any public announcement or press release without the prior circulation to counsel for all of the parties to the MOU, and without the prior review and approval of the Company's legal counsel if by the Plaintiffs, or without the prior review and approval of Co-Lead Counsel for the Plaintiffs in the Actions if by the Company or by the Company or by the Director Defendants, which approval shall be communicated to the Company's legal counsel by Plaintiffs' Co-Lead Counsel in the Illinois Action.

9. The Stipulation may be executed in one or more counterparts. All executed counterparts and each of them shall be deemed to be one and the same instrument. Counsel for the parties to the Stipulation shall exchange among themselves original signed counterparts and a complete set of original executed counterparts shall be filed with the District Court.

10. The Stipulation shall be binding upon, and inure to the benefit of, the successors and assigns of the parties hereto.

11. The District Court shall retain jurisdiction with respect to implementation and enforcement of the terms of the Stipulation, and all parties hereto submit to the jurisdiction of the District Court for purposes of implementing and enforcing the Settlement embodied in the Stipulation.

12. The Stipulation and the Exhibits hereto shall be considered to have been negotiated, executed and delivered, and to be wholly performed, in the State of Illinois and the rights and obligations of the parties to the Stipulation shall be construed and enforced in accordance with, and governed by, the internal, substantive laws of the State of Delaware without giving effect to that State's choice of law principles.

IN WITNESS WHEREOF, the parties hereto have caused the Stipulation to be executed by their duly authorized attorneys, as of May 29, 1997.

Co-Lead Counsel for Plaintiffs
In The Illinois Action

LAW OFFICES OF TERRY ROSE SAUNDERS

/s/ Terry Rose Saunders
TERRY ROSE SAUNDERS, ESQ.

[Counsel Listing Omitted]

EXHIBIT A

I. *Board Structures and Policies*

The Board of Directors shall have appropriate structures and policies to ensure that the Board acts at all times in the best interests of the Company and its shareholders. The Company looks to outside directors to provide an independent view of the performance of the Company and its management. Accordingly, to ensure the highest standards of independent judgment and accountability, a majority of the Board shall be comprised of outside directors.

Outside and Nonmanagement Directors Defined. An "outside director" means a director who

(a) is neither a current employee nor a former member of senior management of the Company or an affiliate;

(b) does not have any business or professional relationship with the Company, either personally or through a company of which the director is an officer or a controlling shareholder, that is material to the Company or to the director;

(c) does not have a close family relationship, by blood, marriage, or otherwise with any member of senior management of the Company or one of the Company's affiliates;

(d) is not an officer of a company of which the Company's chairman or chief executive officer is also a board member;

(e) is not personally receiving compensation from the Company in any capacity other than as a director; and

(f) does not personally receive or is not an employee of a foundation, university, or other institution that receives grants or endowments from the Company, that are

material to the Company or to either the recipient and/or the foundation, university, or institution.

A "*nonmanagement director*" means a director who is not a current employee of the Company.

Management and the Board. The Chief Executive Officer should be a member of the Board of Directors. In order to ensure the greatest number of outside directors on a board of manageable size, other direct management representation should be kept to a minimum and should in no event exceed two other management directors.

The Board of Directors shall make clear to senior management of the Company that board membership is neither necessary to their present positions nor a prerequisite to a higher management position in the Company. Attendance of management staff at Board Meetings should be at the discretion of the Chairman but should be encouraged by the Board. The Board should have full and direct access to members of senior management and should be encouraged to request reports directly to the Board by any member of senior management. Board members should use judgment in dealings with management so that they do not distract management from the business operations of the Company.

Conflicts of Interest. A director's personal financial or family relationships may occasionally give rise to that director's material personal interest in a particular issue. There will be times when a director's material personal interest in an issue will limit that director's ability to vote on that issue. The Board of Directors shall determine whether such a conflict of interest exists on a case-by-case basis. The Board shall take appropriate steps to identify such potential conflicts and to ensure that a majority of the directors voting on an issue are both disinterested and independent with respect to that issue.

"*Senior Management*" includes the chief executive, chief operating, chief financial, chief legal and chief account-

ing officers, president, vice president(s), treasurer, secretary and the controller of the Company.

"*Affiliate*" includes any person or entity which, alone or by contractual obligation, owns or has the power to vote more than twenty-five (25) percent of the equity interest in another, unless some other person or entity acting alone or with another by contractual obligation owns or has the power to vote a greater percentage of the equity interest. A subsidiary is considered an affiliate if it is at least eighty (80) percent owned by the Company and accounts for at least twenty-five (25) percent of the Company's consolidated sales or assets.

II. *Nominating Committee for 1997 Board Elections*

The Nominating Committee for selecting the directors to be proposed for election at the 1997 Annual Meeting shall be comprised of outside directors who were first elected to the Board of Directors after June 25, 1995.

III. *Amendment to By-Laws*

The provisions pertaining to the Board's structures and policies, set forth in Section I, will become part of ADM's By-Laws. Any changes to these provisions will be reported within thirty (30) days of their effective date on Form 8-K of the Securities and Exchange Commission attaching a copy of such amendments, and a copy of such amendments will be filed promptly with the New York Stock Exchange.

IV. *Leadership of the Board*

If the offices of the Chairman and Chief Executive Officer are combined in one person, or if the Chairman is not an outside director, then the outside directors shall annually elect one of their members to serve as Vice-Chairman. The Vice-Chairman shall preside over all meetings of nonmanagement directors and of the Governance

Committee. If the Chairman is an outside director, the Chairman will fulfill these functions.

V. *Independent Review Responsibilities of the Audit Committee*

The Board will charge the Audit Committee with the task of overseeing matters of legal compliance, including issues of potential discrimination, foreign corrupt practices act enforcement, environmental conduct, federal securities laws and disclosure requirements, and determining whether the company is engaged in any anticompetitive activities which would subject the Company to criminal and/or civil prosecution under state or federal antitrust laws.

The Board will charge the Audit Committee with the additional tasks of assuring that corporate information gathering and reporting systems exist which represent a good faith attempt to provide senior management and the Board with information respecting material acts, events or conditions within the Company. Such additional systems, if any, determined appropriate by the Audit Committee shall be implemented within nine (9) months of receiving the Board's Charge unless the Board extends the time in the exercise of its business judgment.

The Audit Committee shall consist solely of outside directors. For a period of three (3) years from the date of this Agreement, the Audit Committee shall consist of outside directors who were first elected to the Board of Directors after June 25, 1995.

The Audit Committee will promulgate, and have the authority to ensure adherence to, policies and procedures regarding compliance with the law, the Company's procedures for circulating these policies and for educating employees regarding compliance with these policies. Senior corporate officers shall report on a regular basis, not

less than three (3) times a year, to the Audit Committee regarding compliance with ADM's policies and procedures and all federal and state laws. The Audit Committee will report regularly, not less than three (3) times a year, to the Board of Directors regarding the effectiveness of the Company's policies and procedures. The Audit Committee will be assisted by outside independent counsel (who will be selected by the Audit Committee) who will be paid from the settlement proceeds fund created by this action for a period of at least three (3) years from the date of Final Court Approval of this Agreement.

The Company will not abolish the office of Corporate Compliance Officer unless the Audit Committee recommends its abolition and the Board approves its abolition.

VI. *Governance Committee*

The Board will create a permanent committee, consisting of the nonmanagement directors, to meet together at least annually to assess Board and Committee effectiveness and to report the results to the Board. The Governance Committee will establish and approve performance criteria for evaluation of the Chief Executive Officer, and all nonmanagement directors should participate in the actual evaluation of the Chief Executive Officer. The performance criteria and evaluation process shall be disclosed to shareholders in the Company's proxy statement for the annual shareholders' meeting.

VII. *Director Remuneration*

At least one-half of the Compensation for non-employee directors will be paid in ADM stock. For a period of three (3) years hereafter, total compensation for each director shall not exceed $100,000 per annum. The valuation of the stock will occur on the last day of the Company's fiscal year.

VIII. *Confidential Voting*

All proxies, ballot and voting tabulations that identify how shareholders voted are to be kept confidential, except: (i) to allow the independent election inspectors to certify the results of the vote; (ii) as necessary to meet applicable legal requirements, including the pursuit or defense of judicial actions; or (iii) in the event of any contested solicitation. The tabulators and the inspectors of election shall be independent and not the employees of ADM.

IX. *Audit, Compensation, Nominating and Succession Committees*

The Company will establish separate Audit, Compensation, Nominating and Succession Committees. The Audit, Compensation, and Nominating Committees shall be comprised exclusively of outside directors. The Succession Committee shall be comprised of a preponderance of outside directors.

X. *Public Policy Committee*

The Public Policy Committee shall be charged with the task of overseeing social responsibility of the Company and shall encourage the Company to communicate on such issues with institutional investors, analysts and other appropriate organizations.

EXHIBIT B-1

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISRICT OF ILLINOIS
URBANA, ILLINOIS

[Caption Omitted in Printing]

NOTICE OF HEARING ON PROPOSED SETTLEMENT OF DERIVATIVE ACTIONS

TO: ALL CURRENT HOLDERS OF ARCHER DANIELS MIDLAND COMPANY COMMON STOCK

PLEASE READ THIS NOTICE CAREFULLY; IT MAY AFFECT YOUR RIGHTS

THIS NOTICE RELATES TO A PROPOSED SETTLEMENT OF SHAREHOLDERS' DERIVATIVE ACTIONS AND CLAIMS ASSERTED THEREIN.

CURRENT HOLDERS OF ARCHER DANIELS MIDLAND COMPANY COMMON STOCK ARE ENTITLED TO OBJECT, IF THEY DESIRE, TO THE SETTLEMENT OF THE DERIVATIVE CLAIMS AS DESCRIBED HEREIN. IF THE COURT APPROVES THE DERIVATIVE SETTLEMENT, YOU WILL BE BARRED FROM CONTESTING THE FAIRNESS, REASONABLENESS OR ADEQUACY OF THE PROPOSED SETTLEMENT, AND FROM PURSUING THE SETTLED DERIVATIVE CLAIMS.

This Notice is given pursuant to Rule 23.1 of the Federal Rules of Civil Procedure and an Order of the United States District Court for the Central District of Illinois (the "Court"). The purpose of the Notice is to advise you that the above-entitled actions (the "Litigation") are now pending in the Court and the Delaware Chancery

Court (the "Delaware Court") and that all parties to the Litigation have reached a settlement (the "Settlement") which would fully, finally and forever resolve the Derivative Claims as between Plaintiffs and the Defendants, as defined herein, on the terms and conditions summarized in this Notice.

This Notice is not intended to be and should not be construed as an expression of any opinion by the Court with respect to the truth of the allegations of the Derivative Claims or the merits of the claims or defenses asserted. This Notice is merely to advise you of the pendency and proposed Settlement of the Derivative Claims and of your rights thereunder.

I. THE LITIGATION

This Litigation was commenced in July 1995, with the filing of purported derivative actions in the United States District Court for the Northern District of Illinois, the Circuit Court of Cook County, Illinois and the Delaware Court. The actions filed in Illinois were transferred to the Court, and plaintiffs filed a Consolidated and Amended Derivative Complaint, entitled *Paul Felzen, Trustee of Louise Laskin Trust—1991 and Sandra Esner, Plaintiffs, v. Dwayne O. Andreas, et al., Defendants, and Archer Daniels Midland Company, Nominal Defendant,* Case No. 2279 (the "Illinois Action"). The Plaintiffs in the Delaware Court filed an amended and consolidated complaint entitled *In: Re Archer Daniels Midland Company Derivative Litigation,* Consolidated No. 14403 (the "Delaware Action"). Both the Illinois Action and the Delaware Action (the "Actions" or the "Litigation") named as defendants Dwayne O. Andreas, Ralph Bruce, John H. Daniels, Howard G. Buffett, Lowell W. Andreas, James R. Randall, Michael D. Andreas, H.D. Hale, O. Glenn Webb, Martin Andreas, Margaretta Rockefeller, F. Ross Johnson, Ray A. Goldberg, John K. Vanier, Shreve M.

Archer, Jr., M. Brian Mulroney, and Robert S. Strauss, and the Delaware Action also named Gaylord O. Coan as a defendant (the "Director Defendants"). The Actions alleged, among other things, that the Director Defendants breached their fiduciary duties or obligations owed to the Company and the stockholders of the Company by participating in improper conduct or failing to properly supervise the activities of certain employees of the Company who had engaged in improper conduct, including violations of federal antitrust laws and federal securities laws.

II. PRETRIAL PROCEEDINGS AND DISCOVERY IN THE LITIGATION

A. *Defendants' Actions*

The Director Defendants and the Company have filed motions to dismiss the Actions. In their motions to dismiss, the Director Defendants and the Company argue that Plaintiffs, among other things, failed to make a demand upon the directors of ADM as required by Delaware law before bringing their action and failed to state a claim for relief against the Director Defendants. Plaintiffs opposed the motions. The motions to dismiss are being held in abeyance pending a hearing by the Court at which this Stipulation and the Settlement are to be presented.

After the announcement of the federal government's investigation into the charges that ADM had violated the antitrust laws and the filing of these Actions, the Company's Board of Directors appointed a Special Committee consisting of outside directors to investigate the charges made by the federal government and undertook certain actions in the areas of corporate governance, employee conduct, compliance, and succession.

ADM's Board of Directors also created the Corporate Governance Committee, consisting of outside directors to

examine, among other things, director qualifications and independence from management. In the Spring of 1996, the Company announced that certain of its directors, including Michael D. Andreas, would not stand for re-election. In April, 1997, the Company announced that Dwayne Andreas had retired from his position as CEO of the Company and that G. Allen Andreas, Jr. would become the CEO and a member of the Board. In addition, the Company announced the election of Ambassador Andrew Young to the Board and the retirement of Lowell Andreas from the Board.

B. *Discovery, Investigation And Research Conducted By Plaintiffs*

Counsel for Plaintiffs have conducted certain discovery and conducted an extensive investigation during the prosecution of the Litigation. Co-Lead Counsel for Plaintiffs in the Illinois Action consulted extensively with experts in the areas of corporate governance and economics and with the Company's largest institutional investors and reviewed and analyzed treatises, articles and authoritative reports on corporate governance issues. In addition, all Plaintiffs' Counsel reviewed and analyzed thousands of pages of documents produced by Defendants, reviewed and analyzed the Company's public filings and press releases, and thoroughly analyzed and evaluated the facts supporting Plaintiffs' claims.

III. THE PROPOSED SETTLEMENT

Based on Plaintiffs' investigation, Plaintiffs have agreed with ADM that it is in the best interests of ADM and its shareholders to settle the derivative claims on the terms of the Stipulation of Settlement. The following description of the proposed Settlement is only a summary, and reference is made to the text of the Stipulation of Settlement, on file with the Court, for a full statement of its provisions:

(i) In Settlement of the derivative claims, the Director Defendants will pay or cause to be paid the total sum of $8 Million to ADM.

(ii) As additional consideration for Settlement of the Litigation, the Board of Directors has also agreed to adopt, upon approval by the Court of the Settlement the corporate governance measures and procedures which are set forth in Exhibit A which is attached to this Notice.

(iii) If the proposed Settlement is approved by the Court, the Court will enter a judgment which will dismiss the derivative claims as against the Director Defendants with prejudice, and all shareholders of ADM shall be barred and enjoined from asserting any Settled Claims, as this term is defined in the Stipulation of Settlement (*i.e.*, causes of action involving breaches of fiduciary duties relating to the allegations in this Litigation) against the Director Defendants or ADM and each and all shareholders shall conclusively be deemed to have released any and all such Settled Claims as against the Director Defendants and ADM.

(iv) All the claims that the Company may have against Michael Andreas, Terrance Wilson, Mark Whitacre, Reinhard Richter, Sidney Hulse and Marty Allison, are reserved to the Company and are not released by the Stipulation of Settlement, nor are they Settled Claims.

(v) Legal counsel for the Plaintiffs in the Actions may make application to the Court for an award of attorney fees, expenses and costs. The Company and the Director Defendants agree not to oppose an application(s) for an award of attorney fees, costs and expenses which does not exceed 49% of the Settlement Proceeds deposited in the Escrow Account, plus interest.

IV. NOTICE TO BANKS, BROKERS, AND OTHER NOMINEES

(a) Banks, brokerage firms, institutions, and other persons who are nominees who currently hold the common stock of ADM for the beneficial interest of other persons are requested within ten (10) days of receipt of the Notice, to forward a copy of the Notice to each such beneficial purchaser and provide the Company with written confirmation that the notice has been so forwarded. Your reasonable costs and expenses of complying with this provision will be paid upon submission of appropriate documentation to the Company. Additional postage prepaid copies of the Notice may be obtained from the Company for forwarding to such beneficial owners. All such correspondence to the Company should be addressed as follows:

Christine Ferguson
ADM
P.O. Box 1470
Decatur, IL 62525
217-424-5656

V. THE HEARING

(b) A hearing (the "Settlement Hearing") will be held before the Honorable Harold A. Baker, United States District Judge, United States District Court, Central District of Illinois, on July 7, 1997, at 9:30 a.m. at the United States Courthouse, 201 South Vine Street, Urbana, Illinois for the purpose of determining (1) whether the proposed Settlement is fair, reasonable and adequate and whether it should be approved by the Court; (2) whether, thereafter, this Litigation should be dismissed with prejudice as set forth in the Stipulation of Settlement dated as of May 29, 1997, on file with the Court; and (3) the reasonableness of the application of plaintiffs' counsel for the payment of attorneys' fees and reimbursement of costs and expenses incurred in connection with this Litigation.

The Settlement Hearing may be continued or adjourned from time to time by the Court at the Settlement Hearing or any continued or adjourned session thereof without further notice.

(c) Any current shareholder of ADM may appear at the Settlement Hearing to show cause why the proposed Settlement should not be approved or why a judgment should or should not be entered thereon; provided, however, that no such person shall be heard, unless his or her objection or opposition including the basis therefor is made in writing and is filed, together with copies of all other papers and briefs to be submitted by him or her to the Court at the Settlement Hearing, with the Court no later than July 3, 1997, and showing due proof of service on Plaintiffs' Co-Lead Counsel:

SPECTOR & ROSEMAN, P.C.
ROBERT M. ROSEMAN, ESQ.
2000 Market Street, 12th Floor
Philadelphia, PA 19103
215-864-2400

LAW OFFICES OF TERRY ROSE SAUNDERS
TERRY ROSE SAUNDERS, ESQ.
30 North LaSalle Street
Suite 3200
Chicago, IL
312-346-4456

and Counsel for ADM:

A. JAMES SHAFTER, Esq.
KEHART, SHAFTER & HUGHES
500 First of America Center
Decatur, IL 62525
217-428-7950

Unless otherwise ordered by the Court, any shareholder of ADM who does not make his or her objection or opposition in the manner provided shall be deemed to have waived all objections and opposition to the fairness, reasonableness and adequacy of the proposed Settlement.

VI. EXAMINATION OF PAPERS AND INQUIRIES

This notice contains only a summary of the terms of the proposed Settlement. For a more detailed statement of the matters involved in this action, reference is made to the pleadings, to the Stipulation of Settlement and to other papers filed in this action which may be inspected at the Office of the Clerk of the United States District Court, United States Courthouse, 201 South Vine Street, Urbana, IL, during business hours of each business day.

Inquiries regarding this action should be addressed as follows:

SPECTOR & ROSEMAN, P.C.
ROBERT M. ROSEMAN, ESQ.
2000 Market Street, 12th Floor
Philadelphia, PA 19103
215-864-2400

DO NOT CONTACT THE COURT REGARDING THIS NOTICE

DATED: May 30, 1997

BY ORDER OF THE COURT
UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF ILLINOIS

ERRATA SHEET

The Notice unintentionally omits the following information: The only claims which are being settled in the District Court are those which have been made in the Illinois Action. Upon approval of the Settlement by the District Court, Co-Lead Counsel in the Delaware Action will apply to dismiss that Action based on the Settlement and will not apply to the Delaware Court for fees and expenses. The inclusion of the Delaware caption in the Notice is not intended to imply to the contrary.

Inquiries regarding this action should be addressed as follows:

SPECTOR & ROSEMAN, P.C.
ROBERT M. ROSEMAN, ESQ.
2000 Market Street, 12th Floor
Philadelphia, PA 19103
215-864-2400

ZWERLING, SCHACHTER & ZWERLING, LLC
SUSAN SALVETTI, ESQ.
767 Third Avenue, 22nd Floor
New York, New York 10017
212-223-3900

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

Case No. 95-2279
Honorable Harold A. Baker
Judge Presiding

PAUL FELZEN, TRUSTEE OF LOUISE LASKIN TRUST—1991 and SANDRA ESNER,
Plaintiffs,
v.
DWAYNE O. ANDREAS, *et al.*,
Defendants,
and
ARCHER DANIELS MIDLAND COMPANY,
a Delaware Corporation,
Nominal Defendant.

SUMMARY NOTICE OF DERIVATIVE LITIGATION SETTLEMENT

TO: ALL CURRENT HOLDERS OF ARCHER DANIELS MIDLAND COMPANY COMMON STOCK:

YOU ARE HEREBY NOTIFIED that the parties to the above litigation have entered into a Stipulation of Settlement (the "Stipulation") with Defendants to resolve the issues raised in the Derivative Claims against the Defendants.

PLEASE BE FURTHER ADVISED that pursuant to an Order of the United States District Court for the

Central District of Illinois, dated May 30, 1997, that a Hearing will be held on July 7, 1997 at 9:30 a.m. before the Honorable Harold A. Baker at the United States Courthouse located at 210 South Vine Street, Urbana, Illinois for the purpose of determining (1) whether the proposed settlement of the Derivative Claims against Defendants as set forth in the Stipulation of Settlement dated as of May 29, 1997, on file with the Court, should be approved by the Court as fair, reasonable and adequate to ADM and its common stockholders; (2) whether, thereafter, the Derivative Claims should be dismissed with prejudice pursuant to the terms of the Stipulation of Settlement; and (3) the reasonableness of the application of plaintiffs' counsel for the payment of attorneys' fees and reimbursemet of costs and expenses incurred in connection with this Litigation, together with interest thereon. If you are a shareholder of ADM, your rights may be affected by the settlement of this action.

If you currently own ADM common stock and have not received a Notice of Hearing on Proposed Settlement of Derivative Action, you may obtain copies by contacting:

ROBERT M. ROSEMAN, ESQ.
SPECTOR & ROSEMAN, P.C.
2000 Market Street, 12th Floor
Philadelphia, PA 19103
215-364-2400

TERRY-ROSE SAUNDERS, ESQ.
LAW OFFICES OF TERRY ROSE SAUNDERS
30 North LaSalle Street, Suite 3200
Chicago, IL 60602
312-346-4456

Co-Lead Counsel for Plaintiffs

or

A. James Shafter, Esq.
KEHART, SHAFTER & WEBBER, P.C.
500 First of America Center
P.O. Box 871
Decatur, IL 62525
Cousel for ADM

PLEASE DO NOT CONTACT THE COURT OR THE CLERK'S OFFICE.

Dated: May 30, 1997

BY ORDER OF THE UNITED STATES DISTRICT COURT FOR THE CENTRAL DISTRICT OF ILLINOIS

[Filed May 30, 1997]

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF ILLINOIS

[Caption Omitted in Printing]

ORDER PRELIMINARILY APPROVING SETTLEMENT AND PROVIDING FOR NOTICE

Whereas, derivative claims are pending before the court in the case entitled *Paul Felzen, Trustee of Louise Laskin Trust—1991 and Sandra Esner vs. Dwayne O. Andreas, et al., and Archer Daniels Midland Company,* Case No. 95-cv-2279 (the "Illinois Action") and similar derivative claims are pending before the Delaware Court of Chancery in *In re Archer Daniels Midland Company,* Consolidated C.A. No. 14403 (the shareholders' derivative claims are collectively referred to as the "derivative claims"), and

Whereas, the parties to the Illinois Action have applied to the court, pursuant to Rule 23.1 of the Federal Rules of Civil Procedure for an order approving the settlement of the Illinois Action and resolution of the Delaware claims in accordance with the Stipulation of Settlement, dated May 29, 1997 (the "Stipulation"), which, together with the exhibits annexed thereto, sets forth the terms and conditions for a proposed settlement of the derivative claims and for dismissal of the Illinois Action as against the defendants upon the terms and conditions set forth therein; and the court having read and considered the Stipulation and the exhibits annexed thereto;

NOW, THEREFORE, IT IS HEREBY ORDERED:

1. This order (the "Preliminary Approval Order") hereby incorporate by reference the definitions in the Stipulation, and all terms used herein shall have the same meanings as set forth in the Stipulation;

2. The court hereby preliminarily approves the Stipulation and the settlement described therein as being fair, reasonable and adequate to ADM and its shareholders;

3. A hearing (the "Settlement Hearing") shall be held before the undersigned United States District Judge on July 7, 1997 at 9:30 a.m., at the United States Courthouse, Central District of Illinois, 201 South Vine Street, Urbana, Illinois to determine whether the proposed settlement of the derivative claims on the terms and conditions provided in the Stipulation is fair, reasonable and adequate and should be approved by the court; whether a judgment, as provided in ¶ F.1.b. of the Stipulation should be entered herein; and to determine whether plaintiffs' counsels' fees and expenses should be approved;

4. The court hereby approves, as to form and content, the Notice of Hearing on Proposed Settlement of Derivative Action (the "Notice"), and the Summary Notice for Publication (the "Summary Notice") annexed as exhibits B-1 and B-2 attached to the Stipulation. The court finds that the publication, mailing and distribution of the Notice and the Summary Notice substantially in the manner and form set forth in ¶ 5 of this order meets the requirements of Fed.R.Civ.P. 23.1 and due process, and is the best notice practicable under the circumstances and shall constitute due and sufficient notice to all persons who are entitled thereto.

5. The cost of notice to shareholders will be paid in accordance with ¶ B.2. of the Stipulation. The Company is hereby authorized to supervise and administer the giving of notice as set forth below;

(a) On or before May 30, 1997, the Company shall mail or cause to be mailed copies of the notice substantially in the form annexed to the Stipulation as exhibit B-1 to all current shareholders of record of ADM as of May 29, 1997, who can be identified with reasonable effort;

(b) On or before June 13, 1997, the Company shall cause a Summary Notice, substantially in the form an-

nexed to the Stipulation as exhibit A-2, to be published once in the national edition of *The Wall Street Journal*;

(c) At or prior to the Settlement Hearing provided for in ¶ 3 of this order, a representative on behalf of the Company shall serve and file with the court proof by affidavit of such publication and mailing.

6. Nominees who currently hold ADM stock as of May 29, 1997, shall send the Notice to all beneficial owners of such ADM common stock within 10 days after receipt of the Notice.

7. Any shareholder of record of ADM as of May 29, 1997, may appear and show cause, if he, she or it has any, why the proposed settlement of the derivative claims embodied in the Stipulation should or should not be approved as fair, reasonable and adequate, or why a judgment should or should not be entered thereon; provided, however, that no shareholder of ADM or any other person shall be heard or entitled to contest the approval of the terms and conditions of the proposed settlement, or, if approved, the judgment to be entered thereon approving the same, unless on or before July 3, 1997, that person has served by hand, or by first class mail delivered on said date, written objections, including the basis therefor, and copies of any papers and briefs in support of their position upon Robert M. Roseman, Esq. Spector & Roseman, P.C., 2000 Market Street, 12th Floor, Philadelphia, PA 19103 and Terry Rose Saunders, Law Offices of Terry Rose Saunders, Esq., 30 North LaSalle Street, Suite 3200, Chicago IL 60602, Co-Lead Counsel for Plaintiffs; and A. James Shafter, Esq., Kehart, Shafter & Hughes, 500 First Amer ca Center, Decatur, Illinois, 62525, counsel for ADM, and said objections, papers and briefs have been received by the Clerk of the court. Co-lead Counsel for plaintiffs shall immediately serve by facsimile and overnight mail copies of any written objections and any papers and briefs served upon them to Susan Salvetti, Esq., Zwerling, Schachter & Zwerling, LLP, 767

Third Avenue, New York, NY 10022. The above listed counsel will give prompt notice of any such objections received to other counsel on their respective side of the case. Any shareholder of ADM who does not make his, her or its objection in the manner provided for herein, shall be deemed to have waived such objection and shall forever be foreclosed from making any objection to the fairness or adequacy of the proposed settlement as incorporated in the Stipulation, unless otherwise ordered by the court.

8. Upon the effective date, all shareholders of ADM and ADM shall be barred from asserting any settled claims, as defined in the Stipulation, and each and all shareholders of ADM and ADM shall conclusively be deemed to have released any and all such settled claims, and all claims which the Company has against the Excluded persons, as defined in the Stipulation, or may have against Andreas and Wilson, as defined in the Stipulation, are not settled claims and shall be reserved to the Company in its sole discretion.

9. All papers in support of the settlement and for reimbursement of attorneys' fees and expenses shall be filed at least 7 days prior to the settlement hearing.

10. The court reserves the right to continue or adjourn the date of the settlement hearing and any continuance or adjournment thereof without further notice to the shareholders of ADM and retains jurisdiction to consider all further applications arising out of or connected with the proposed settlement.

Enter this 30th day of May 1997.

/s/ Harold A. Baker
HAROLD A. BAKER
Senior United States District Judge

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

[Caption Omitted in Printing]

OBJECTION TO PROPOSED SETTLEMENT OF DERIVATIVE ACTIONS

COME NOW, Charles W. Pauly, Jr. and Elizabeth D. Pauly, joint tenants and file this Objection to Proposed Settlement of Derivative Actions and would show to the Court as follows:

1. If the Plaintiffs' case *has merit*, then the financial settlement is grossly inadequate to compensate the Plaintiffs for the injuries suffered as a result of the actions by the Defendants.

2. If the Plaintiffs' case *is without merit*, then the case is being settled for nuisance value which compensates Plaintiffs' attorneys, but does nothing to enhance shareholder value. In fact, it only demonstrates the company is a "soft" target for future frivolous litigation.

3. Plaintiffs should be put to trial and demonstrate the merits of their claim. If Plaintiffs are successful, then damages will be substantially higher than the nominal consideration being received in the settlement. If Plaintiffs are unsuccessful, the suit was without merit and the Plaintiffs and their counsel should receive nothing.

WHEREFORE, premises considered, movant requests the Court deny the proposed settlement as being unfair and inadequate to the shareholders of Archer Daniels Midland Company.

/s/ Charles W. Pauly
CHARLES W. PAULY
517 South Main Street
P.O. Box 409
Carthage, Missouri 64836
(417)358-4049 Telephone

[Certificate of Service Omitted in Printing]

[Filed Jun 26, 1997]

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

[Caption Omitted in Printing]

OBJECTION OF MITCHELL BERNS TO AWARD OF EXCESSIVE ATTORNEYS' FEES

MITCHELL BERNS states for his objection to an award of excessive attorneys' fees:

1. I own 600 shares of ADM common stock through a profit sharing account at PaineWebber. My residence is 201 N Street, N.W., Apt. 702, Washington, D.C. 20037. I am employed as the Director of the Office of Supervision at the Federal Housing Finance Board, a federal regulatory agency in Washington. Previous to my government employment, I practiced law in New York City, including the representation of plaintiffs and defendants in securities class actions.

2. I have no specific knowledge regarding the facts or the court file, and take no position on the merits of the proposed settlement. It appears from the Notice of Settlement Hearing ("Notice") I received in the mail that the settlement comprises an $8 million payment by defendant directors to the company and the adoption of certain common sense corporate governance controls and procedures, of the sort that a public corporation might well be inclined to adopt irrespective of allegations of wrongdoing.

3. The Notice indicates that the defendants have agreed not to oppose a fee award of up to 49% of the

setttlement fund. This action is two years old. It appears that little formal discovery was taken, and that the settlement comes at an early stage in the proceedings. Although plaintiffs' counsel are to be commended for pursuing the matter, it would appear difficult to justify a fee award of more than 15-20% of the settlement proceeds under the circumstances. A proposed settlement including a 49% no-objection clause raises concerns about potential over-reaching on its face.

4. Securties class actions, diligently pursued, can be an effective mechanism for the enforcement of shareholder rights. However, fee awards that appear excessive in light of the benefit achieved undermine public confidence in the courts and in the efficacy of the derivative and class action mechanism.

5. I therefore respectfully request that the Court make a fee award that fairly compensates plaintiffs' counsel, yet takes due account of the results achieved by the settlement.

[Proof of Service Omitted in Printing]

I declare under penalty of perjury that the foregoing is true and correct.

/s/ Mitchell Berns
MITCHELL BERNS

Dated: June 23, 1997

110 Daryl Ave.
Novato, CA 94947

June 23, 1997

Honorable Harold A. Baker
Judge Presiding
In the United States District Court
For the Central District of Illinois
Urbana, Illinois

Dear Judge Baker:

I am writing about Case No. 95-2279, Paul Felzen, Trustee of Louise Laskin Trust—1991 and Sandra Esner V. Dwayne O. Anderas [*sic*], Et. Al., and Archer Daniels Midland Company.

I am a shareholder of Archer Daniels Midland Company. I have received an eight page package from the attorneys and have responded to them.

My concern is that the legal counsel for the Plaintiffs may request up to 49% of the Settlement Proceeds. Additionally the agreement states the Defendants agree not to oppose an application(s) for an award of such amount. The legal counsel for Plaintiffs now has a conflict of interest with the Plaintiffs. Please exercise your judicial powers and only award to counsel a fair amount. To me, 49% seems excessive and should not be allowed.

Sincerely,

/s/ John P.Chiara
JOHN P. CHIARA

TWO MONTAGUE TERRACE
BROOKLYN, NEW YORK 11201-4105

June 19, 1997

Hon. Harold A. Baker
United States District Court Judge
U.S. District Court House
201 South Vine Street
Urbana, Il 61801

Ref Paul Felzen, Trustee v. A.D.M.
Case no. 95-2279

Dear Judge Baker,

As an A.D.M. shareholder of record (1042 shares, which are in my account with Dean Witter), I received notice of a proposed settlement of the above case.

At least one aspect of the proposed settlement deserves your close scrutiny: attorney fees, costs and expenses not to exceed 49 pct. of the settlement proceeds.

I have to say that I am in the shipping business, as a chartering broker, where my firm works, sometimes for weeks, setting up charters, for 1.25 pct. of the freight charges on an ocean shipment. Usually the freights are $300,000 or $400,000, yielding us say $3000 to $5000 per charter. Real estate brokers get 10 or maybe 15 pct. commissions, and that is, I believe often split between brokers. 49 pct is beyond any normal conception, and I urge you to substantially reduce the percentage of the settlement fees to the attorneys.

It crosses my mind that there are law firms in both Philadelphia and Chicago, and maybe in Delaware, involved in this case. When I am trying to arrange a charter, the market dictates that I involve as few brokers and thus as few commissions payable as possible, and

I think that law firms should be encouraged to act similarly whenever possible. You hold the possibility of such encouragement in your hands.

The irony of a suit brought on behalf of shareholders, the results of which are eaten away at 49% for attorneys fees will, I am sure, not have escaped you.

Very truly yours,

/s/ Peter D. Scott
PETER D. SCOTT

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

[Caption Omitted in Printing]

AFFIDAVIT OF SUSAN SALVETTI IN SUPPORT OF THE PROPOSED SETTLEMENT AND THE PETITION OF DELAWARE PLAINTIFFS' COUNSEL FOR ATTORNEYS' FEES AND REIMBURSEMENT OF EXPENSES

STATE OF NEW YORK)
) ss. :
COUNTY OF NEW YORK)

Susan Salvetti, being duly sworn, deposes and says:

1. I am an attorney duly admitted to practice law before the courts of the State of New York, as well as the United States District Courts for the Southern and Eastern Districts of New York, and for the Central District of Illinois. I am a member of the law firm of Zwerling, Schachter & Zwerling, LLP, which, together with Wechsler Harwood Halebian & Feffer LLP and Bernstein Liebhard & Lifshitz, constitute co-lead counsel for plaintiffs in the matter: *In Re: Archer Daniels Midland Company* (Consolidated C.A. No. 14403) pending in the Court of Chancery of the State of Delaware (the "Delaware Action"). As such, I have personal knowledge of the matters set forth herein based upon my supervision and participation in this litigation as a co-lead counsel.

2. This affidavit is submitted in support of the proposed settlement reached and encompassed by a Stipulation of Settlement, dated May 29, 1997, entered by and

among: (i) the plaintiffs in the above-encaptioned matter, *Paul Felzen, Trustee of Louis Laskin Trust—1991, et ano v. Dwayne O. Andreas, et al., Defendants, and Archer Daniels Midland Company, Nominal Defendant,* pending in this Court (the "Illinois Action"), and the plaintiffs in the Delaware Action, on behalf of themselves, as shareholders of nominal defendant Archer Daniels Midland Company ("ADM" or the "Company") and derivatively on behalf of ADM, (ii) the Director Defendants, defined in paragraph 5 below, and (iii) Nominal Defendant, ADM ("Stipulation of Settlement"). This affidavit is also submitted in support of the application by plaintiffs' counsel in the Delaware Action ("Delaware Counsel") for an award of attorneys' fees and expenses in the amount of $2,664,000 (representing 33⅓% of the $8 million Settlement Fund), to be apportioned equally between plaintiffs' counsel in the Delaware and Illinois Actions, rather than the application by Illinois plaintiffs' counsel for an award of attorneys' fees, costs and expenses in the amount of up to 49% of the $8 million Settlement Fund, or $3,920,000.

3. The Stipulation of Settlement, together with the exhibits annexed thereto, represents the terms and conditions of the proposed settlement, which was preliminarily approved by this Court after a hearing on May 30, 1997. At that time, the Order Preliminarily Approving Settlement and Providing for Notice was entered (the "Order"). On June 13, 1997, a Summary Notice of Settlement appeared in the national edition of *The Wall Street Journal.* In addition, pursuant to the Order, notices have been sent to all current shareholders of record of ADM as of May 29, 1997 ("Record Shareholders"). To date, over 243,000 notices have been sent, yet only five objections have been received, discussed *infra.*

4. This affidavit sets forth the facts that demonstrate that the proposed settlement is fair, reasonable and adequate to ADM and its shareholders and should be approved. When viewed against the risk of establishing demand futility pursuant to Delaware Chancery Rule 23.1, and overcoming the 8 Del. Ch. § 102(b)(7) exculpatory provision in ADM's Certificate of Incorporation, the proposed settlement is outstanding in the context of both the value of its therapeutic benefits, particularly those pertaining to corporate compliance issues, as well as its monetary benefits.

I.

Events Leading to the Proposed Settlement

5. The Delaware Action was commenced in July 1995 with the filing of numerous individual shareholder derivative suits, against Dwayne O. Andreas, Michael D. Andreas, Lowell W. Andreas, Martin L. Andreas, H. D. Hale, James R. Randall, Ralph Bruce, John H. Daniels, Shreve M. Archer, Jr., Ray A. Goldberg, John K. Vanier, Gaylord O. Coan, M. Brian Mulroney, Margaretta Rockefeller, O. Glenn Webb, F. Ross Johnson, Howard G. Buffett and Rober S. Strauss (the "Director Defendants"), all current or former directors of ADM. At the same time, ADM shareholders filed the Illinois Action. By mid-September 1995, there were thirteen derivative suits filed in Delaware.

6. On September 21, 1995, an organizational meeting of all Delaware Counsel was held wherein my firm, together with the firms of Wechsler, Harwood, Halebian & Feffer, LLP and Bernstein, Liebhard & Lishitz were elected plaintiffs' co-lead counsel ("Delaware co-lead counsel") with the authority, *inter alia,* to monitor, supervise and coordinate all aspects of the litigation.

7. On October 10, 1995, Delaware co-lead counsel traveled to Washington, D.C. at the request of Williams & Connolly, counsel for ADM in the Delaware Action. At the meeting, it was agreed that to avoid unnecessary duplication of discovery, Delaware Counsel, to the extent practicable, would coordinate and participate in the dis-

covery then being organized in connection with various antitrust and securities class action cases brought against ADM; however, such participation would not preclude Delaware Counsel from seeking additional discovery regarding the pending derivative issues.

8. By Order of Consolidation dated March 3, 1996, all of the Delaware derivative actions were consolidated for all purposes, and the Court approved the appointment of Delaware co-lead counsel. It was further ordered that as soon as practicable, a consolidated amended complaint would be filed and that Plaintiffs' First Request for Production of Documents filed in one of the individual Delaware actions would be designated as plaintiffs' First Document Request.

9. At all times following the Court of Chancery's March 3, 1996 Order, Delaware Counsel conducted informal discovery of the facts involved in the Delaware Action. As relevant news about ADM appeared almost daily, Delaware Counsel began drafting a consolidated amended derivative complaint, while also preparing third-party discovery requests directed to the Department of Justice. Subpoenae were also prepared and served upon certain foreign competitors alleged to have been involved in price fixing activities with ADM. Delaware Counsel also further investigated and drafted memoranda analyzing and summarizing the inter-relationships (personal and business) between and among the Director Defendants which we believed were instrumental in developing evidence supporting the allegations that the Director Defendants breached their duty of loyalty, and lacked independence such that pre-suit demand was futile.

10. In May 1996, I was advised by Williams & Connolly, that the first wave of document production by ADM was being organized in Chicago and that, subject to counsels' execution of a confidentiality stipulation, document review would begin in or about June or July.

11. Document review began the week of July 8, 1996, with a team of fourteen lawyers on behalf of the Delaware Action reviewing over one hundred boxes of documents produced by ADM in Chicago. A second session was held in September 1996, which included the review of an additional seventy boxes of documents.

12. At the end of September 1996, Delaware co-lead counsel learned that a settlement had been reached in the ADM securities class action. To ensure that the terms of that settlement could not be construed to release any pending derivative claims, Delaware co-lead counsel prepared and forwarded to securities class counsel specific language preserving the derivative claims for inclusion in that settlement.

13. Following the news in mid-October 1996 that ADM had pled guilty to criminal price-fixing charges, Delaware co-lead counsel filed its Amended and Consolidated Derivative Complaint on November 19, 1996, which included all events that had occurred in 1996.

14. The Amended and Consolidated Derivative Complaint alleged, among other things, that the Director Defendants had breached their fiduciary duties of good faith, loyalty, and care owed to ADM and its stockholders by, among other things, failing to supervise the activities of ADM officers, and by failing to implement and maintain internal systems of control and compliance to detect violations of the law.

15. On December 12, 1996, ADM served its notice of motion to dismiss the Amended and Consolidated Derivative Complaint. Thereafter, through January and the beginning of February 1997, five separate motions to dismiss with supporting memoranda of law were filed by the following defendant groups: (1) defendants Archer, Bruce, Coan, Daniels, Goldberg, Hale, Johnson, Mulroney, Rockefeller, Strauss, Vanier and Webb; (2) nominal defendant ADM; (3) defendant Randall; (4) the Andreas defendants; and (5) defendant Buffett.

16. The focus of the motions to dismiss in the Delaware Action was directed to three primary issues: pre-suit demand pursuant to Delaware Chancery Rule 23.1, whether plaintiffs stated a claim for breach of fiduciary duty pursuant to Chancery Rule 12(b)(6), and whether ADM's adoption of exculpatory provisions in its Certificate of Incorporation required dismissal of the complaint pursuant to 8 Del. Ch. § 102(b)(7). Thus, the Director Defendants and the Company argued that: the Delaware plaintiffs had not met their burden of establishing demand futility; the Delaware plaintiffs had not stated a claim for relief; and pursuant to Delaware law, 8 Del. Ch. § 102 (b)(7), the defendants could not be held liable, as a matter of law, for any of the breaches of duty alleged in the Amended and Consolidated Derivative Complaint.

17. While opposition to the motions to dismiss was being finalized, Delaware co-lead counsel were asked to attend a meeting with Robert Roseman, Esq. and Terry Rose Saunders, Esq., co-lead counsel in the Illinois Action (collectively "Illinois co-lead counsel"). For the first time, Delaware co-lead counsel learned that settlement negotiations had been held between the parties in the Illinois Action, to the exclusion of the Delaware plaintiffs.

18. On April 30, 1997, Delaware co-lead counsel met with Illinois co-lead counsel in New York. At that meeting, Mr. Roseman advised us that settlement negotiations in the Illinois Action had been ongoing since December 1996. and that the parties had reached an agreement in principle. Mr. Roseman summarized the terms of the agreement and requested that Delaware co-lead counsel seriously consider joining in the agreement since, in his opinion, negotiations were near completion. At the conclusion of the meeting, Delaware co-lead counsel requested that a copy of the term sheet, described by Mr. Roseman as Exhibit "A" to the Memorandum of Understanding (then being drafted), be produced for our review and analysis.

II.

Enhancements to the Proposed Settlement Procured by Delaware Counsel

19. Following a series of daily conversations with counsel for ADM regarding production of the term sheet, it was produced to Delaware co-lead counsel pursuant to a letter agreement of confidentiality on May 5, 1997. Upon review of the term sheet, one of the Delaware co-lead counsel, Stanley Bernstein, Esq., recognized that it was patterned after the settlement in *In re Sears Shareholder Litigation*, No. 88CH/0009 (Cir. Ct. Cook Cty., Ch. Div. 1988), which he personally had developed.

20. As presented, the provisions of the term sheet provided a framework for settlement; however, Delaware co-lead counsel remained concerned that, among other things, important issues of corporate compliance—going to the very heart of the Delaware Action—remained unaddressed and unresolved. Accordingly, following review of various treatises and articles regarding corporate governance and compliance, consultation with an expert, as well as communications with a large institutional investor of ADM, negotiations began between Delaware co-lead counsel and counsel for ADM, as well as the Director Defendants, to address and incorporate clarifications, changes and additional protections into the settlement to enhance its benefits and satisfy Delaware co-lead counsels' concerns.

21. Notwithstanding the position of some ADM counsel that negotiations as to the provisions of the term sheet were "closed", Delaware co-lead counsel refused to agree to the term sheet, despite the risk that a settlement might be approved without regard to the concerns or claims of the Delaware plaintiffs.

22. During the next twenty-four days, Delaware co-lead counsel were involved in daily, intensive negotiations with counsel for ADM and the Director Defendants, in-

cluding two face-to-face meetings in Delaware and Chicago. Illinois co-lead counsel played no active role in these meetings.

23. Three primary issues provided the focal point of these arm's-length negotiations: first, as to corporate compliance, Delaware co-lead counsel sought agreement by the Director Defendants and ADM to implement an information gathering and reporting system which would provide senior management and ADM's Board of Directors (the "Board") with knowledge of material acts, events or conditions within the Company; a reporting system between senior corporate officers and a Committee of the Board regarding compliance with ADM's policies and procedures and all federal and state laws; and, in turn, a reporting system between that Committee and the entire Board as to the effectiveness of the Company's policies and procedures. As to these points, counsel for ADM acknowledged our concerns, and were amenable to making meaningful enhancements to the agreement to allay those concerns. Thus, language was incorporated into the term sheet to require that such systems would exist within the Company. As a result, Section V of the term sheet requires that a reporting system must be established to provide direct communication between senior management and the Audit Committee, as well as between the Audit Committee and the Board. Senior management must report on a "regular basis" of "not less than three (3) times a year" regarding "compliance with ADM's policies and procedures and all federal and state laws," and the Audit Committee must report to the Board, on the same regular basis, regarding "the effectiveness of the Company's policies and procedures." Thus, as a result of Delaware counsels' efforts, the Audit Committee's compliance duties are proactive rather than reactive.

24. As detailed in the accompanying affidavit of Professor James L. Bicksler, an expert in the areas of financial economics and corporate governance, active corporate compliance in the form of monitoring and reporting between the board of directors and senior management is a most basic responsibility of an effective board. Such complicance systems are thus crucial to establish a strong corporate structure as well as to foster shareholder prosperity. That is exactly what, among other things, the proposed settlement now accomplishes. (The affidavit of Professor Bicksler is annexed hereto as Exhibit "A").

25. Second, Delaware co-lead counsel required, and it was agreed, that various provisions regarding corporate governance procedures be compulsory in nature, rather than permissive. In the opinion of Delaware co-lead counsel, defendants' agreement was particularly significant, because for example, a majority of the Board "shall" be comprised of outside directors; the Board "shall" have appropriate structures and policies to ensure that it acts in the best interest of the Company and its shareholders; the Board "shall" determine whether any conflict of interest exists between a director's personal interest in an issue and his ability to vote, the Board "shall" take appropriate steps to identify such potential conflicts, and ensure that a majority of the directors voting on an issue are both distinterested and independent with respect to that issue. (*See also* Bicksler affidavit ¶¶ 37, 38 and 41). Third, as to the definition of "outside" director, Delaware co-lead counsel sought, and it was agreed, that any relationship between a director "by blood or marriage" with a member of senior management would be deemed a "close family relationship" for purposes of exclusion of that person on the board as an outside director.

26. Agreement regarding all of the foregoing terms was finally reached on May 28, 1997, at which time Delaware co-lead counsel signed the Memorandum of Understanding ("MOU"). The Stipulation of Setttlement encompassing the terms of the MOU as agreed to on May 29, 1997. Delaware co-lead counsel has had no negotiation with

counsel for Director Defendants or ADM regarding the payment of fees and/or expenses.

III.

The Benefits Of The Proposed Settlement Versus The Risks of Continued Litigation

27. There is no doubt on the part of Delaware Counsel that, if approved by this Court, the proposed settlement will confer upon ADM substantial benefits, particularly in the area of corporate compliance, which, in turn, will benefit ADM shareholders. It is respectfully submitted that the proposed settlement is an excellent result because it addresses and resolves the very issues raised in both the Illinois Action and Delaware Action regarding board supervision, monitoring, reporting, and independence, as well as provides for a monetary fund (paid for on behalf of the Director Defendants by their insurance carriers) to finance (among other things) implementation of many of the corporate compliance procedures and mechanisms. Thus, the proposed settlement confers substantial benefits, at no cost to the Company.

28. When compared with the result reached through the proposed settlement, continuing the litigation would be extremely risky to plaintiffs in view of the arguments and supporting case law raised by the Director Defendants and the Company in their motions to dismiss. Although Delaware plaintiffs believe that their claims have merit, issues such as demand futility and the exculpatory § 102 (b)7 provision always foster a certain degree of uncertainty as to whether derivative claims will survive dismissal. There is never a guarantee that plaintiffs will be successful in convincing the Delaware Court that demand is futile, or that the conduct of defendants, as pled, is not shielded by the exculpatory provision contained in ADM's Certificate of Incorporation. Accordingly, Delaware co-lead counsel believe that the proposed settlement is in the

best interests of ADM shareholders, and should be approved.

IV.

The Fee Petition

29. Delaware co-lead counsel did not negotiate the fee and expense award requested by Illinois plaintiffs' counsel —*i.e.*, up to 49% of the $8 million Settlement Fund, or $3,920,000. Delaware co-lead counsel submit that an award of 49% of the Settlement Fund would seriously deplete the Settlement Fund and impair the Audit Committee's ability to perform its functions in connection with the implementation of the programs, procedures and measures required by the proposed settlement.

30. Rather, as set forth above, Delaware co-lead counsel request that a total fee (including expenses) be awarded in the amount of $2,664,000, representing 33⅓% of the $8 million Setttlement Fund amount. Delaware Counsel further request that the total award be allocated equally between Delaware and Illinois plaintiffs' counsel, or $1,332,000 to each, plus interest.

31. As fully set forth above, as well as in the accompanying Memorandum on Behalf of Delaware Plaintiffs in Support of the Proposed Settlement and Award of Fees and Expenses (the "Memo"), Delaware Counsel submit that not only is a 33⅓% award fair and reasonable, but also that an equal division of the award is similarly fair and reasonable in this situation where there is no basis to elevate the contributions made by one set of lawyers over the other. The mere fact that Illinois co-lead counsel had been negotiating with defendants and ADM counsel prior to Delaware co-lead counsels' knowledge or involvement, should not in any way detract from the substantial contributions which Delaware Counsel have made to the proposed settlement. Indeed, the length of time spent in negotiations should not be the sole measure of the degree or value of the contribution made. Instead, warranted here is the recognition that all counsel devoted their best

efforts, with equal vigor and diligence, to achieve an excellent result through their respective contributions. Thus, an equal division of the award should be granted.

32. As shown in the accompanying Memo, determination of a fair fee must also include consideration of the contingent nature of counsels' retainer and of the extent of the difficulties and uncertainties which were overcome in obtaining the settlement.

33. Here, counsel agreed to prosecute this case on a wholly contingent basis. Counsel knew from the outset that they might expend hundreds of thousand [*sic*] of dollars worth of attorneys' time in pursuing this action, yet receive no compensation whatsoever if the action ultimately proved unsuccessful.

34. This affidavit and the Memo describe the substantial risks of litigation. Those same difficulties also constitute risks that counsel might never be paid for their efforts.

35. As detailed in the individual affidavits of Delaware Counsel, Exhibits "1" through "21" contained in the accompanying Appendix to this affidavit (the "Appendix"), professionals in the firms representing Delaware plaintiffs collectively expended over 4,959.36 hours since the inception of the Delaware Action through May 30, 1997, with no assurance of success. In addition, Delaware Counsel have expended a total of over $103,203.81 in unreimbursed expenses (see Exhibits "1" through "21" in the Appendix). Although a litigation fund created in the Delaware Action, to date, holds $16,154.86, it is anticipated that those funds will be depleted to pay for the expenses incurred in connection with Delaware co-lead counsels' appearance in Urbana for the Settlement Hearing, as well as expenses incurred in the preparation of this application, including photocopying and secretarial overtime. A breakdown by law firm involved in the Delaware Action of fees and expenses through May 30, 1997, is as follows:

	Law Firm	Hours	Lodestar	Expenses
1.	Bernstein Liebhard & Lifshitz	1,089.25	$361,756.25	$16,822.15
2.	Weschler Harwood Halebian & Feffer LLP	1,117.60	357,084.00	15,971.00
3.	Zwerling, Schachter & Zwerling, LLP	1,265.00	408,119.50	26,056.28
4.	Berman, DeValerio & Pease, LLP	47.90	13,720.50	1.075.57
5.	Jeffrey Boxer Associates	31.00	10,850.00	83.00
6.	Burt & Pucillo	159.75	50,955.00	4,627.51
7.	Finkelstein, Thompson & Loughran	243.50	78,968.75	5,558.80
8.	Gilman & Pastor	47.00	13,410.00	1,971.18
9.	Girard & Green, LLP	13.50	4,725.00	1,623.90
10.	Gordon & Kaplan	59.91	19,568.50	603.00
11.	Law Offices of James V. Bashian	124.20	39,845.00	2,266.89
12.	Law Offices of A. Arnold Gershon, P.C.	8.25	3,506.25	00.00
13.	Law Offices of Charles J. Piven, P.A.	8.20	2,706.00	1,110.95
14.	Law Offices of Miles M. Tepper	96.50	39,897.50	3,985.90
15.	Law Offices of Curtis V. Trinko, LLP	84.90	21,539.50	4,327.26
16.	Meyers & Milewski, P.C.	67.00	17,575.00	306.00
17.	Phillips, Goldman & Spence, P.A.	52.50	9,206.50	898.36
18.	Pomerantz Haudek Block & Grossman	33.00	10,500.00	1,775.66
19.	Rosenthal, Monhait, Gross & Goddess, P.A.	100.65	33,640.00	2,659.70
20.	Schoengold & Sporn, P.C.	124.75	44,901.25	4,389.89
21.	Schubert & Reed, LLP	185.00	48,868.00	7,090.81
	TOTAL	4,959.36	1,591,342.50	103,203.81

For their investment of time and effort over the course of the past two years, Delaware Counsel will recover only 77% of their actual time, assuming this Court grants Delaware Counsels' petition.

36. The expertise and experience of counsel is another important factor in setting a fair fee. The expertise and experience of plaintiffs' counsel in the Delaware Action is also described in Exhibits "1" through "21" in the Appendix. As shown therein, Delaware Counsel are experienced and skilled practitioners in the securties litigation field, and are responsible for numerous significant settlements, as well as legal decisions that enable litigation such as this to be successfully prosecuted.

37. Courts have repeatedly held that it is in the public interest to have experienced and able counsel enforce the regulations pertaining to the duties of officers and directors of public companies. Vigorous private enforcement of state corporation laws can only occur if private plaintiffs can obtain parity representation with that available to large institutional interests. If this imporant public policy is to be carried out, the courts must award fees which will adequately compensate private plaintiffs' counsel, taking into account the enormous risks undertaken with a clear view of the economics of a contingent derivative action.

38. When Delaware Counsel undertook to act for the plaintiffs in the Delaware Action, it was with the knowledge that we would spend many hours of hard work against some of the best defense lawyers in the United States with no assurance of ever obtaining any compensation for our efforts, or even for the overhead of our offices, which is an increasingly substantial consideration. We were aware that the only way we would be compensated was to achieve a successful result. The benefits conferred by this proposed settlement are particularly noteworthy in that they resolve the core issues of both the Delaware Action and Illinois Action despite the existence

of substantial risk and the vigorous defense mounted by the Director Defendants and the Company. Thus, it is respectfully submitted that Delaware Counsels' fee petition be granted.

V.

Objections Received To The Proposed Settlement

39. As stated above, over 243,000 notices were mailed to ADM Record Shareholders; only five objections to the proposed settlement have been received.

40. Objectors John P. Chiara, Peter D. Scott and Mitchell Berns assert that a fee and expense award equaling 49% of the Settlement Fund (or $3,920,000) would be excessive. Mr. Berns further asserts that 15-20% of the Settlement Fund would be an adequate fee award. However, as set forth above, Delaware Counsel have expended time and expenses which exceed the award that we seek. In any event, Delaware Counsel submit that based on all of the foregoing, a fair and reasonable fee and expense award of the Settlement Fund with an equal allocation between counsel for Delaware plaintiffs and counsel for Illinois plaintiffs.

41. Objectors Charles W. Pauly, Jr. and Elizabeth D. Pauly (the "Pauly Objection") assert, in the alternative, that if plaintiffs' case has merit, the monetary portion of the proposed settlement is inadequate; if plaintiffs' case has no merit, they assert, that the proposed settlement does nothing to enhance shareholder value, is being paid for nuisance value, and that the case should, in any event, go to trial.

42. The Pauly Objection reflects a lack of understanding not only of the principal claims asserted in the Delaware Action and the substantial benefit obtained here, but also, of the considerable risks of going forward with the litigation, as detailed above.

43. The bases for the principal claims in the Delaware Action relate to a lack of a corporate compliance system to monitor and oversee employee conduct, as well as a lack of independence of a majority of ADM's board members because of their personal and business inter-relationships. The proposed settlement addresses and resolves those claims. Among other things, it requires that the Board be comprised of a majority of outside directors, it defines what constitutes an outside director, and it requires that a procedure for corporate compliance be instituted in the form of corporate information gathering and reporting regarding compliance with ADM's policies and procedures, as well as compliance with all federal and state laws. In addition, the proposed settlement creates a Settlement Fund of $8 million dollars from which payments are to be made to pay for implementing these new corporate procedures and practices, including payments for outside independent counsel, as well as to pay plaintiffs' counsel in the derivative actions. Most impressive is that the monies paid to the Settlement Fund come from insurance carriers on behalf of the Director Defendants, and not from the Company.

44. To suggest, as the Pauly Objection does, that a trial on the merits is the better alternative than this proposed settlement, lacks the appreciation of the significant legal obstacles Delaware Counsel face in overcoming the motions to dismiss, as well as the substantial benefits obtained through the proposed settlement.

45. Objectors John J. Gilbert and Martin Glotzer assert that the proposed settlement is lacking because it omits a provision adopting cumulative voting procedures. As this objection admits, a proposed provision for cumulative voting appeared in the last proxy statement of ADM and did not receive enough votes to pass. It is submitted that the issue of cumulative voting, as set forth in the objection, is best left to inclusion in a proxy statement

for vote by all shareholders. Since the proposed settlement requires that a majority of the board be outside directors, as defined therein, it is further submitted that concerns regarding a non-independent board have been addressed and resolved.

CONCLUSION

Based on the facts and circumstances of this case, the significant risks and burdens faced by plaintiffs if the Delaware Action were to proceed, and the substantial procedures regarding corporate compliance which the Director Defendants and ADM have agreed to implement, Delaware Counsel believe that the proposed settlement is fair, reasonable and extremely advantageous to the shareholders, is fully supported by the record in this case, and should be approved. Delaware plaintiffs also respectfully request that Delaware Counsels' application for an award of attorneys' fees and reimbursement of expenses in an amount of 33⅓% of the Settlement Fund ($2,664,000) plus interest be granted with an equal allocation between Delaware and Illinois plaintiffs' counsel.

/s/ Susan Salvetti
SUSAN SALVETTI

[Notary and Appendix Omitted in Printing]

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

[Caption Omitted in Printing]

AFFIDAVIT OF PROFESSOR JAMES L. BICKSLER IN SUPPORT OF SETTLEMENT OF ARCHER DANIELS MIDLAND COMPANY LITIGATION

STATE OF NEW YORK)
) ss.:
COUNTY OF NEW YORK)

Professor James L. Bicksler, being duly sworn deposes and says:

I. INTRODUCTION AND SYNOPSIS

1. I am a Professor at Rutgers University—Faculty of Management in the Economics-Finance area and have been at this institution since 1969.

2. The purpose of my Affidavit is to provide corporate governance and shareholder market valuation perspectives relevant to the Archer Daniels Midland Company ("ADM" or the "Company"), including the economic benefits accruing to ADM and its shareholders as a result of the settlement of the derivative actions (the "Settlement"). The discussion of the settlement builds upon and, indeed, is integrated within relevant economic concepts and empirics. Based on economic-financial principles applied to the Settlement, I conclude that the Settlement offers features that will have important long-term benefits for the Company and its shareholders.

3. The organization of the Affidavit is as follows:

Section II discusses my professional qualifications as an expert in the area of financial economics and corporate governance. Section III discusses the nature of the corporation, and the potential conflict between the shareholders and incumbent management. Section IV discusses the roles of the board of directors in corporate governance. A synopsis of some of the relevant literature dealing with the importance of effective corporate governance is provided. A number of interesting empirical observations, including the importance of independent directors, are noted. Section V provides perspectives on both the old structure at ADM. It is noted that the old governance structure at ADM was characterized by cronyism and passivity. As a result of the settlement, there will be an emphasis on independent directors and an information flow from an in-place corporate reporting system. This will result in a much more vibrant corporate governance structure at the Company. Section VI provides an economic understanding of some of the proposed provisions of the settlement and their value-enhancing aspects to the Company and its shareholders. Section VII constitutes the Summary and Conclusions.

II. PROFESSIONAL BACKGROUND

4. My background includes a Ph.D. in finance from New York University. I have previously been a financial economist for Stanford Research Institute, and served on the faculty at the University of Hawaii. I have also been a visiting faculty member at several universities. Also, over the years, I have been a consultant on finance-investment issues for corporations and governments. Articles, notes and reviews of mine have appeared in the *American Economic Review, Journal of Financial Economics, Economics Journal, Journal of Finance, Journal of Financial and Quantitative Analysis* and *Anti-Trust Bulletin* journals. I am editor of several books on finance and investments.

5. While I have a diverse range of interests within financial economics, my particular areas of interest include market valuation of firms and financial securities, corporate governance and institutional investors, and pension fund issues.

6. I have organized or co-organized several Roundtables, Forums and panels on economic and finance issues ranging from corporate governance to corporate finance, corporate strategy and investment strategy. Some sample Roundtables, Forums and Panels have been:

(a) "The Financial Services Industry: Market Changes and Corporate Strategies"

(b) "Corporate Excellence"

(c) "The Fiduciary Responsibilities of Institutional Investors"

(d) "Corporate Governance, Restructuring and the Market for Corporate Control"

(e) "Corporate Takeovers, Restructuring and The Market for Corporate Control"

(f) "Leverage, Workouts and Bankruptcy"

7. Participants in the conferences that I have organized have included such Nobel Prize in Economics recipients as Paul A. Samuelson, Merton H. Miller, Franco Modigliani and James Tobin. Other notables have been Delaware Chancellor William T. Allen; Steven M. H. Wallman, presently a Commissioner at the Securities and Exchange Commission; Peter Peterson, Chairman, The Blackstone Group, and former U.S. Secretary of Commerce; Richard Syron, Chairman and CEO, American Stock Exchange, and former President of the Federal Reserve Bank of Boston; and John Biggs, Chairman and CEO, TIAA-CREF which has a portfolio maket value of $195 billion.

8. I have provided services as an expert in other shareholder litigations, such as *In re Sears Shareholder Litigation*, No. 88 CH/0009 (Circ. Ct. Cook Cty., Chancery Div. 1988). In that litigation I was asked whether that Settlement, which provided for many corporate governance and outsider director provisions similar to those incorporated here, resulted in significant economic benefits to the company and its shareholders. My affidavit was cited with authority by the Court in finding that, as I had opined, these charges were beneficial to Sears.

III. THE NATURE OF THE CORPORATION: AND CORPORATE CONTROL MECHANISMS

9. The modern corporation is a particular business form that has certain economic advantages in organizing production, marketing and finance and, hence, in maximizing the economic welfare of the firm's shareholders.

10. The normative goal of the corporation is to maximize the price of equity shares for its present shareholders. This normative corporate objective obviates the need to take into account the particular consumption tastes and risk preferences of the individual investors or of the institutional common equity shareholders of a given company.

11. Indeed, one economic advantage of the modern corporation is that decision making can be delegated to corporate managers without the need to specifically elicit the risk and investment preferences of each or any of the many diverse shareholders of the firm. Thus, the usefulness of the shareholder maximization rule is that it provides a general structure for rational corporate decision making without incurring the burden of the economic costs of shareholder polling. Indeed, one Nobel Memorial Prize in Economic Sciences awardee, Professor Ronald H. Coase of the University of Chicago—School of Law, gives further insights with regard to why there is a corporate form of business organization. Coase argues (*see* Ronald H. Coase, "The Nature of the Firm," *Economica,*

November, 1937) that the corporate firm arises because of the savings in transaction costs, including monitoring costs, in operatting in a market where information is imperfect.[1]

12. One important characteristic of the large publicly traded corporation is the separation of equity ownership (*i.e.*, risk bearing) and decision making (*i.e.*, resource allocation strategy and tactics). A corollary is that corporate executive management may make decisions that are not in the best interests of the shareholders. Furthermore, the executive management team may continue year after year to act in this manner despite their poor performance, because there is relatively little most investors can do to correct this agency problem.

13. One possible way that the interests of shareholders can be protected is through a board of directors, who recognize their fiduciary responsibilities to shareholders. and have or are provided systematic, directed, and relevant information flow through an in-place corporate reporting system from all levels of the corporation.

IV. THE ROLES OF THE BOARD OF DIRECTORS IN CORPORATE GOVERNANCE

14. As mentioned, the monitoring of management decisions by a board of directors—particularly outside directors who have access to systematic, directed, and relevant information flow through an in-place corporate reporting system from all levels of the corporation—is an important mechanism for protecting the interests of the

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1 Coase answers the question as to why corporations as an organization form exist and continue to persist. Coase's answer is "that firms increase efficiency by minimizing the costs of making and monitoring agreements among employees, suppliers and customers, thereby, in turn, lowering the costs of contracting for goods and services." See L. Gordon Crovitz, "Ronald Coase, Practical Economists: A Nobel Prize for Privatization, Property Rights and Contracts," Barron's, October 28, 1991.

shareholders and making sure executive management performs its fiduciary duties to the shoreholders.

15. Chancellor William T. Allen of the Delaware Chancery Court, and a leading judicial scholar on corporate law, has discussed a board's duty to insure that each director receives information sufficient to satisfy his/her responsibility and that systems be in place to achieve this goal. Specifically in the *Caremark* decision, Chancellor Allen held "it is important that the board exercise a good faith judgment that the corporation's information and reporting system is in concept and design adequate to assure the board that appropriate information will come to its attention in a timely manner as a matter of ordinary operations, so that it may satisfy its responsibility." This is important because, as Chancellor Allen notes, "I am of the view that a director's obligation includes a duty to attempt in good faith to assure that a corporate information and reporting system, which the board concludes is adequate, exists and that failure to do so under some circumstances may render a director liable for losses caused by non-compliance with applicable legal standards." (*See* William T. Allen, *In re Caremark International Inc. Derivative Litigation,* Consolidated Civil Action No. 13670, September 25, 1996.)

16. Dennis Block and Jonathan M. Hoff comment on the *Caremark* decision of Chancellor William T. Allen. They note that board directors do have oversight responsibilities, and that the corporate directors have a duty of care to act on an informed basis, which relates to the presence of information flow and from and in-place corporate reporting system. Thus, the *Caremark* decision points to corporate directors having fiduciary duties to perform monitoring functions based on information flows gathered by corporate in-place reporting systems. (*See* Dennis J. Block and Jonathan M. Hoff, "Duty of 'Caremark' Directors' Oversight Function," *New York Law Journal,* November 21, 1996.)

17. The importance of the *Caremark* decision by Chancellor William T. Allen has been far-reaching. For example, *Caremark* has already effected "proper governance" in the financial services-banking area. In this regard, Mr. Serino, Deputy Chief Counsel—Office of the Comptroller of the Currency, has indicated the importance of an internal ethics compliance program and that "institutions that adopt an effective compliance program can look to a reduction of fines and reduced jail time for its officials over those who don't." (*See* James Del Guerico, *Southern California Business*, April 1, 1997.)

18. In commenting on *Caremark*, it is noted that a "proper" corporate governance framework of today stresses the importance of compliance with particular emphasis on the corporate directors providing an independent check on whether the executive management team has set up an in-house corporate reporting and compliance system. (*See* Richard S. Gruner, "Director and Officer Liability for Defective Compliance: Caremark and Beyond," in Carole W. Basri, Joseph E. Murphy and Gregory J. Wallance, *Corporate Compliance After Caremark*, Practising Law Institute, New York, N.Y., 1997.)

19. The substantial implications of *Caremark* for directors has been pointed out by numerous authors. After all, Chancellor Allen pointed out that "a director's obligation includes a duty to attempt in good faith to assure that a corporate information and reporting system, which the board concludes is adequate, exists, and that failure to do so . . . may . . . render a director liable for losses caused by non-compliance with applicable legal standards." It puts an important responsibility on directors to be accountable for an in-place, two-way compliance reporting system. This means that there are to be regular reports to the director and board, evaluating and assessing its adequacy and any potential problems that might arise from this system.

20. Interestingly, the present Chief Justice of the Delaware Supreme Court, E. Norman Veasey, writing before his appointment had much the same idea that Chancellor Allen stated in *Caremark* inasmuch as he stated:

> "There is a belief that 'recommended corporate practice' involves some monitoring or supervision, at least to ensure compliance with the law. If the expected role of a director has grown to include the installation of mechanisms to endure compliance with laws, good counselling suggests that it be done."

(*See* E. Norman Veasey and Julie M.S. Seitz, "The Business Judgment Rule in the Revised Model Act, the Trans Union Case, and the ALI Project—A Strange Porridge, *Texas Law Review*, 1985.

21. Professor Eugene Fama of the University of Chicago has suggested that external or outside directors may be more effective than internal or inside directors. Professor Fama argues that outside directors are concerned with protecting or enhancing their professional reputations as competent managers and typically owe less allegiance to incumbent management than inside directors. Hence, outside directors are more likely than inside directors *not* to rubber-stamp corporate strategies that might lower the market price of common stock. Thus, Professor Fama's reasoning suggests that the monitoring of corporate performance by outside directors may be a low cost, relatively efficient mechanism for improving corporate governance and firm performance. (*See* Eugene F. Fama, "Agency Problem and the Theory of the Firm," *Journal of Political Economy*, April, 1980.)

22. An important emperical study investigating the differential effect of outside directors versus inside directors in effecting CEO turnover and internal change in corporate control is Michael Weisbach, "Outside Directors and CEO Turnover," *Journal of Financial Economics*, 1988.

23. The Weisbach empirical study is based on a bivaricated sample of firms that are classified as either insider-director dominated or outsider-director dominated. He found that outsider-dominated boards are more prone to monitor incumbent management and to use unfavorable common stock return performance as a basis to remove the incumbent CEO relatively quickly. Professor Weisbach also found that CEO executive management changes result in an increase in equity share prices for companies that have outsider-dominated boards. For insider-dominated boards, such CEO changes do not result in additional positive shareholder value.

24. Thus, the Weisbach and Fama studies provide an economic rationale and empirical support for the general proposition that outsider-dominated boards provide a potentially effective monitoring mechanism.

25. Korn/Ferry International argues that the other important tasks of the board are (1) monitoring financial performance, (2) CEO development, evaluation and succession, (3) monitoring the legal and ethical performance of the corporation and (4) crisis management. (*See* Korn/Ferry International, *Board Meeting in Session*, "Twenty 'Best Practices' Improve Board Performance," New York, N.Y., April, 1997.)

26. The "Keys to Effectiveness" for a board, in the opinion of Korn/Ferry International, are (1) expertise, (2) information, (3) power, (4) motivation and (5) focus.

27. In this regard, Ira Milstein of Weil, Gotshal & Manges has argued "that an independent, attentive board is the grain in the balance that leads to a corporate advantage. A performing board is most likely to respond effectively to a world where the pace of change is accelerating. An inert board is more likely to produce leadership that circles the wagons." (*See* Ira Millstein, *The New York Times*, April 6, 1997.)

28. The conventional view of the responsibilities of corporate directors, in the words of Chancellor William T. Allen, is "badly deficient."

> The conventional perception is that boards should select senior management, create incentive compensation schemes and then step back and watch the organization prosper. In addition, board members should be available to act as advisors to the CEO when called upon and they should be prepared to act during a crisis: an emergency succession problem, threatened insolvency or an MBO proposal, for example.
>
> This view of the responsibilities of membership on the board of directors of a public company is, in my opinion, badly deficient. It ignores a most basic responsibility: the duty to monitor the performance of senior management in an informed way. Outside directors should function as active monitors of corporate management, not just in crisis, but continually; they should have an active role in the formulation of the long-term strategic, financial, and organizational goals of the corporation and should approve plans to achieve those goals; they should as well engage in the periodic review of short and long-term performance according to plan and be prepared to press for correction when in their judgment there is need.

(*See* William T. Allen, Delaware Court of chancery, *Redefining the Role of Outside Directors in an Age of Global Competition*, presented at Ray Garrett, Jr., Corporate and Securities Law Institute, Northwestern University, Chicago, Illinois, April, 1994.)

29. In other words, Chancellor Allen's view of the corporate responsibilities of the board directors includes the duty to monitor the executive management team both broadly and narrowly. This, in turn, requires that there

be systematic, directed, and relevant information flows and the availability, if need be, of a centralized reporting place for employees to report violations of company policy and the law. Obviously, corporate directors have a further need to assimilate this information and act in an informed way to structure and implement strategies and tactics designed to improve the operating results of the company.

30. In summary, corporate boards, if effective, are a tremendously important mechanism to bolster the market price of the stock for the Company and its shareholders. If the corporate directors are effective, then the company will be run efficiently and the shareholders will prosper. This requires, as Chancellor Allen suggests, that there will be systematic, directed, and relevant information flow to the corporate directors and that they take an activist role in strategy formulation and monitoring. If, however, the corporate directors are not effective in formulating and monitoring a meaningful relevant corporate strategy, or in having/creating a systematic, directed, and relevant information flow through a corporate reporting system, and in choosing the best management team to implement the corporate strategy-tactics, the shareholders will suffer a significant wealth loss. Boards are usually more effective from an economic as well as governance standpoint if there are a number of independent, or better yet a majority of independent, board members. However, a corollary of this is that independent directors become much more effective, if there is systematic, directed, and relevant information flow. Indeed, these conclusions concerning the importance of outsider-dominated boards to the company and its shareholders are rigorously established in the literature reviewed in this section. Similarly, the importance of systematic, directed and relevant information flow to outside directors is crucial for outside directors to fulfill their heightened director responsibilities as detailed by Chancellor Allen.

V. THE OLD GOVERNANCE STRUCTURE AT ARCHER DANIELS MIDLAND AND THE NEW GOVERNANCE STRUCTURE AT ARCHER DANIELS MIDLAND

31. The travails of ADM are well known, and have been frequently documented in the financial press in such publications as *Business Week, Fortune, The New York Times* and *The Wall Street Journal.*

32. The core of the events at ADM involved its price-fixing violations. However, beyond the activities leading to its guilty plea with regard to price-fixing, ADM is a sad story of corporate governance gone awry, and one where the board of directors did not fulfill their fiduciary duties.

33. ADM has lacked a systematic, directed and relevant information flow to its directors from senior management relating to the monitoring responsibility of its directors. Indeed, as *Business Week* has noted, the board of directors of Archer Daniels Midland is their pick for the worst board in corporate America. (See John A. Byrne, "The Best and Worst of Boards: Our New Report Card on Corporate Governance," *Business Week,* November 25, 1996.)

34. In addition, the nature of Archer Daniels Midland's problems has, in essence, been a result of a weak, ineffective and incestuous Board of Directors which has failed to exercise its fiduciary duties to put the interest of the corporation and shareholders first.

VI. THE ARCHER DANIELS MIDLAND SETTLEMENT

35. Detailed below is a general description of the Settlement. Specific emphasis is given to the particular provisions of Board Structure and Policies.

36. As to Board Structures and Policies, they deal with a number of issues, including the minimum number

or ratio of outside directors, as well as the definition of what is meant by outside directors, and economic issues involving a conflict of interests or potential conflict of interests.

37. One important provision of the Settlement is that a majority of the board of directors *must* be outside directors. This requirement is far superior to an aspiration; it offers ADM no opportunity or flexibility to circumvent, for whatever reason, the mandate that the majority of directors be outside directors.

38. The definition of outside directors is also specific, rather than simply being vague and ambiguous. It requires that any outside director (1) cannot be a present employee or a former senior executive; (2) does not have any relationship with ADM in a business or professional sense; (3) does not have, with any member of executive management, a relationship via blood or marriage; (4) does not have employment in a company in which the chairman or CEO of ADM is a board member, and (5) does not receive compensation from ADM in any capacity other than that as a director.

39. Another important provision concerns the reporting mechanisms put into place as part of the Settlement. Specifically, senior corporate officers will now be required to report on a regular basis, not less than three times a year, to the Audit Committee regarding compliance with ADM's policies and procedures and all federal and state laws. Additionally, the Audit Committee will report regularly to the full Board of Directors regarding the effectiveness of the Company's monitoring and compliances policies and procedures.

40. The creation of a board having a majority of independent directors, coupled with enhanced board information gathering and reporting systems, has important therapeutic value and value-enhancing consequences for the Company and its shareholders. These provisions will

help ensure that ADM enters the twenty-first century as a model of appropriate corporate governance acting in the best interests of shareholders.

41. Another provision of the Settlement deals with conflict situations involving directors. This provision is anticipatory in the sense that if a potential conflict arises then there is an in-place corporate governance mechanism to deal with this problem. Specifically, this provision indicates that the board of directors will help to anticipate whether there are any possible conflicts of interest. The board will use its judgment to determine on a case-by-case basis whether a board member should be excluded from voting because of a conflict of interest. In all cases where a board vote is required, it shall be the case that the majority of directors will be disinterested and independent regarding the situation where the directors' vote is required.

42. Other important provisions of the Settlement concern the Audit and Governance Committees. The Audit Committee's responsibilities have been enhanced to include monitoring and oversight—*i.e.* whether legal compliance issues have been properly fulfilled. These issues of legal compliance include discrimination, corruption activities in foreign countries environment codes, securities laws, disclosure obligations as well as any anticompetition practices that might lead to criminal or civil prosecution.

43. The composition of the Audit Committee has also been structured in a manner consistent with the principles of "proper" corporate governance. Specifically, the members will consist entirely of outside directors who became board members after June 25, 1995. It will have its own separate outside counsel, which will be hired by this Committee and will have full authority with regard to issues surrounding the law.

44. Another equally important provision is the creation of a Governance Committee. The members of this

Committee will consist of all nonmanagement directors. Its task will be to set performance standards and criteria to evaluate the actual performance of ADM's Chief Executive Officer. The standards and criteria used to evaluate the actual performance of the CEO will be published in the proxy statement for the annual meeting of shareholders.

45. These provisions will result in the Settlement achieving substantial improvements in the governance structure and thus in the accountability of ADM's CEO and executive management. This will likely lead to significantly improved operating cost and economic profit-cash flow performance at ADM and its associated business units. Ergo, it will result in a corporate strategy that will increase the market price of ADM's common stock. Alternatively stated, the Settlement will confer substantial economic benefits upon the Company and its shareholders by better aligning the economic interests of the Company's Board of Directors and the Company's executive management with those of the Company's common shareholders. This will establish a pragmatic basis on which the financial markets can be confident that the ADM executive management team will undertake strategy decisions for the benefit of the Company and its common shareholders. Hence, there will be a higher market price particularly in the long run for ADM common stock as the benefits from improved corporate governance and a value enhancing corporate strategy are made more apparent to investors through the information flows to the financial markets and the reality of these benefits is made apparent to all investors.

46. Interestingly, in my 1991 *Sears* Affidavit submitted to examine the impact of substantially similar corporate governance changes to Sears, Roebuck, my economic assessment of the impact of the changed governance structure was that there were substantial long-run benefits that would flow to the company and the Sears shareholders

from the *Sears* Settlement. This assessment was on target and, in retrospect, predictive of what occurred to the stock price. Alternatively stated, in the Sears litigation, I maintained that there would be substantial economic benefits conferred to the shareholders in the long run as a result of this Settlement. As the *actual* time series of common stock prices of Sears has unfolded, my economic benefit assessment has been uncannily accurate.

47. In the *Sears* case, some of the essential corporate goveranance changes were similar to those here. For example, there was an emphasis on adding new and additional outside directors and that at least 75% of the Board had to be comprised of outside directors and that the key committees were made to be comprised of independent, outside directors. In fact, the foundation of this Settlement was modeled on the *Sears* Settlement that was structured with my assistance. The one important change in the Settlement has been the addition of the corporate information system dimension that is a result of Chancellor Allen's decision in *Caremark*. Specifically, the Settlement has the additional substantial benefit of a systematic, directed, and relevant information flow and in-place corporate reporting system enhancing the effectiveness of the outside board members and the corporate governance structure at ADM.

48. In my *Sears* affidavit, I opined that there was substantial long-term economic benefits that would accrue to the Sears and the shareholders as a result of the Settlement. This economic conclusion is even stronger in the instant case because of the additional benefits obtained here in light of the *Caremark* decision.

VII. SUMMARY AND CONCLUSIONS

49. This Affidavit has presented my economic assessments, as well as the underlying analytical and empirical reasoning why the Settlement confers significant economic benefits upon both the Company and its shareholders.

50. The effectiveness of a corporate governance and compliance structure depends critically on the board of directors. The literature, specifically the Fama and Weisbach papers, provides both the economic rationale and empirical evidence supportive of the importance of outside directors in an effective governance structure.

51. The ADM board of directors has historically been characterized by a weak and ineffective governance structure leading to actions detrimental to the Company and its shareholders.

52. The Settlement improves in several important aspects their governance structure because the board is now required to be comprised of a majority of outside directors. Further, the provisions characterizing the definition of what constitutes an outside director are operationally specific and not open to debate. Also, the corporate governance structure of ADM has been improved through an anticipatory recognition of potential conflicts of interest and the putting in place of an appropriate mechanism for recognizing and dealing with conflicts of interest at the board of directors.

53. Additionally, a systematic, directed, and relevant information flow and in-place corporate reporting system enhances the effectiveness of the outside board members and the corporate governance structure at the Company.

54. Likewise, the Audit and Governance Committees have been structured both in terms of the availability of information and sufficient committee power to make significant contributions that benefit the Company and the shareholders.

55. These important governance structure changes will improve the functioning of ADM's board in meeting its duty of care and in meeting mandates such as good faith attempts to estabilsh corporate information and reporting systems that are contained in Chancellor Allen's decision in the *Caremark* litigation.

56. In summary, the Settlement confers significant corporate governance benefits, which in my opinion will translate into positive long-term value for ADM and its shareholders.

/s/ James L. Bicksler
JAMES L. BICKSLER

[Notary and References Omitted in Printing]

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IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

[Caption Omitted in Printing]

MOTION FOR FINAL APPROVAL OF THE PROPOSED SETTLEMENT AND PLAINTIFFS' COUNSEL'S JOINT APPLICATION FOR AN AWARD OF ATTORNEYS' FEES AND REIMBURSEMENT OF EXPENSES

Plaintiffs, by their attorneys, move this Court to enter the Final Judgment and Order of Dismissal, a copy of which is attached to this Motion as Exhibit 1, and the Order Approving Plaintiffs' Counsel's Application for Fees, attached as Exhibit 2, and in support of their Motion, state as follows:

1. On May 30, 1997, the Court entered the Order Preliminarily Approving Settlement and Providing For Notice (the 'Preliminary Approval Order") which preliminarily approved the Stipulation of Settlement (the "Settlement") entered into by and between counsel for the parties to the above-captioned action (the "Litigation") and counsel to a similar action pending in the Delaware Court of Chancery as *In Re Archer Daniels Midland Company Derivative Litigation*, Consolidated No. 14403 (the "Delaware Action").

2. Pursuant to the Preliminary Approval Order, a notice (the "Notice") of the Settlement was mailed to over 243,000 current shareholders of Archer Daniels Midland Co. ("ADM") and a summary notice was published in *The Wall Street Journal* on June 13, 1997.

3. The Notice set July 7, 1997 as the date for a hearing to determine whether the proposed Settlement should

be approved as fair, reasonable and adequate to ADM and its shareholders and whether the Judgment approving the Settlement should be entered and to consider Plaintiffs' Counsel's application for an award of attorneys' fees and reimbursement of expenses, and any objections to the Settlement, the Final Judgment or Plaintiffs' Counsel's application for an award of fees and expenses.

4. Plaintiffs submit the following documents in support of this Motion:

a) Joint Declaration of Terry Rose Saunders and Robert M. Roseman in Support of the Proposed Settlement and Plaintiffs' Counsel's Joint Application for An Award of Attorneys' Fees and Reimbursement of Expenses;

b) Plaintiffs' Memorandum in Support of the Proposed Settlement; and

c) Plaintiffs' Memoradum in Support of Plaintiffs' Counsel's Joint Application For An Award of Attorneys' Fees and Reimbursement of Expenses.

WHEREFORE, plaintiffs move this Court to enter the Final Judgment and Order of Dismissal and the Order Awarding Plaintiffs' Counsel's Fees and Reimbursement of Expenses.

Dated: June 30, 1997

Respectfully submitted,

[Counsel Listing Omitted in Printing]

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

[Caption Omitted in Printing]

JOINT DECLARATION OF TERRY ROSE SAUNDERS AND ROBERT M. ROSEMAN IN SUPPORT OF THE PROPOSED SETTLEMENT AND PLAINTIFFS' COUNSEL'S JOINT APPLICATION FOR AN AWARD OF ATTORNEYS' FEES AND REIMBURSEMENT OF EXPENSES

Terry Rose Saunders and Robert M. Roseman declare as follows:

I. INTRODUCTION

1. Terry Rose Saunders is a principal in the firm of Law Offices of Terry Rose Saunders and Robert M. Roseman is a partner in the firm of Spector & Roseman, P.C. Ms. Saunders and Mr. Roseman ("Plaintiffs' Co-Lead Counsel") have been actively involved in the prosecution of this litigation, are fully familiar with the proceedings, and, if called upon, are competent to testify to the matters set forth in this Declaration.

2. We submit this Declaration in support of (a) the proposesd settlement (the "Settlement") of this derivative action between plaintiffs, Paul Felzen, Trustee of Louise Laskin Trust—1991 and Sandra Esner, as shareholders of Archer Daniels Midland Company, nominal defendant Archer Daniels Midland Company ("ADM") and the seventeen individual defendants who were directors of ADM when the events that led to this litigation occurred ("the Director Defendants"), and (b) plaintiffs' counsel's joint application for an award of attorneys' fees and reimbursement of expenses.

3. The parties have entered into this Settlement in good faith and after extended arms-length negotiations by experienced and informed counsel. This Declaration, the Affidavit of John C. Coffee ("Coffee Affidavit") and the Declaration of R. Alan Miller ("Miller Declaration") provide factual support for the conclusion of plaintiffs and their counsel that the Settlement is fair, reasonable and adequate.

4. After two years of litigation, including a hard-fought motion to dismiss and six months of settlement negotiations, the parties have agreed to a Settlement that will result in benefits for ADM and its shareholders that go beyond those which plaintiffs could have achieved through litigation. The Settlement will result in substantial changes in the composition and functioning of ADM's Board of Directors and key Committees. These structural changes are designed to prevent recurrence of ADM's recent problems and change the public perception of ADM.

5. Specifically, the corporate governance measures require ADM to maintain a Board of Directors without ties to management that will be expected to exercise independent judgment and monitor corporate conduct effectively. These measures also require the Audit Committee to take specific steps to ensure that ADM complies with the law. Moreover, the Settlement creates an $8 million fund to be paid from the Directors and Officers Liability Insurance (the "Settlement Proceeds") for the Company to pay for these benefits, including independent outside legal counsel to assist the Audit Committee in its legal compliance tasks, and to pay any award of attorneys' fees and reimbursement of expenses made by this Court.

6. The Settlement is an outstanding result for ADM and its share holders. Not only did plaintiffs face legal and factual obstacles to ultimate success on the merits, but even if successful, they faced the prospect of no recovery. Any amount plaintiffs could hope to recover from the defendants would pale in comparison to the hundreds of millions of dollars ADM has had to spend as the result of its antitrust problems. This Settlement assures that ADM will promptly adopt measures that approximate the "state of the art" in American corporate governance today and will help guard against the significant financial liability that could result from having corporate officers violate criminal or civil laws in the future.

7. This Declaration also provides factual support for the request of Plaintiffs' counsel for an award of attorneys' fees of 40 percent ($3,200,000) of the Settlement Proceeds, and reimbursement of expenses of $76,501.69 to be paid from the Settlement Proceeds. As explained in the Miller Declaration, this amount is a small percentage (2 percent) of the total value of the benefit obtained for ADM and its shareholders (conservatively $158 million). It is also less than the amount of attorneys' fees and expenses that ADM has agreed not to oppose.

8. The fairness and adequacy of the Settlement and plaintiffs' counsel's request for fees and expenses are confirmed by the favorable response to the Settlement to date by ADM shareholders. Over 243,000 Notices of the hearing on the Settlement have been mailed to ADM's shareholders. As of June 27, 1997, five objections to the Settlement or the award of attorneys' fees have been received.

II. HISTORY OF THE LITIGATION

A. *Background Events.*

9. Two years ago, agents of the Federal Bureau of Investigation and the Antitrust Division of the Department of Justice arrived at the homes of numerous ADM executives and managers and ADM's corporate headquarters. The government sought documents to support

its ongoing, but previously undisclosed, investigation into charges that ADM was fixing prices of citric acid, high-fructose corn syrup ("HFCS") and lysine. Two weeks later, *The Wall Street Journal* reported that the FBI had been investigating ADM since 1992, when Mark Whitacre, a senior executive of ADM, approached the FBI concerning price fixing activities in which he claimed to be involved at ADM. Early reports stated that the government had videotaped Michael Andreas, the Company's Vice-Chairman and son of Dwayne Andreas, ADM's Chairman and Chief Executive Officer, and Terrance Wilson, President of the ADM Corn Processing Division and Group Vice President, meeting with competitors to discuss plans to limit the production of lysine. These press reports further disclosed that Howard Buffett had resigned from ADM's Board of Directors in early July "because he was troubled by the investigation and the way the Company was handling it", and because he had "lost confidence in whether he was being accurately informed by other [ADM] executives about the details of the antitrust matter." This news fueled concern about whether ADM, long criticized for being run as a "family fiefdom" of Dwayne Andreas, would respond appropriately to the investigation.

10. Shortly after the government investigation was disclosed, purchasers of ADM's lysine, high-fructose corn syrup and citric acid brought civil antitrust class actions alleging that ADM and others had violated the federal antitrust laws by agreeing to fix prices and allocate or limit production. In addition, ADM shareholders commenced class actions against ADM and certain officers for violating the federal securities laws by misrepresenting the Company's earnings, profitability, results of operations and business prospects in connection with the sale of ADM's common stock. ADM's common stock price had dropped approximately 15% from $18.625 per share on June 26, 1995, the day before the FBI raids, to $14.28 per share on July 10, 1995.

11. Whitacre had also alleged that ADM rewarded top executives with foreign pay deposited in overseas accounts. According to Whitacre, these so-called slush funds were part of a Company policy and were common knowledge to senior executives.

B. *Plaintiffs Commence This Action.*

12. The plaintiffs in this action are current shareholders of ADM who also held ADM stock in June 1995. Plaintiff Paul Felzen, Trustee of Louise Laskin Trust—1991, filed his complaint on July 11, 1995 in the United States District Court for the Northern District of Illinois. Plaintiff Sandra Esner filed her complaint on the same date in the Circuit Court of Cook County, Illinois. Deidra Graulich filed a second federal court complaint on July 12, 1995, in the Northern District of Illinois. On August 7, 1995, defendants removed the *Esner* Action to the United States District Court for the Northern District of Illinois.

13. The derivative complaints alleged that the Director Defendants breached their fiduciary duties to the Company and its stockholders by causing ADM to violate federal antitrust and securities laws and failing to monitor ADM's operations and employees to prevent violations of the law. On August 4, 1995, the defendants moved to transfer the *Felzen* and *Graulich* actions to the Central District of Illinois. Defendants added the *Esner* action after it was removed. Plaintiffs opposed the transfer.

14. After conducting significant additional research and analysis of publicly available information about ADM and its directors, plaintiffs Felzen and Esner filed a Proposed Consolidated and Amended Derivative Complaint (the "First Consolidated Complaint") on September 29, 1995, and named as defendants Dwayne O. Andreas, Ralph Bruce, John H. Daniels, Howard G. Buffett, Lowell W. Andreas, James R. Randall, Michael D. Andreas,

H.D. Hale, O. Glenn Webb, Martin Andreas, Margaretta Rockefeller, F. Ross Johnson, Ray A. Goldberg, John K. Vanier, Shreve M. Archer, Jr., M. Brian Mulroney and Robert S. Strauss (the "Director Defendants"). The First Consolidated Complaint alleged that the Director Defendants (1) breached their fiduciary duties by participating in illegal price-fixing or not properly monitoring ADM's personnel and operations to prevent illegal price-fixing and illegal foreign payments and (2) grossly mismanaged ADM.

15. The First Consolidated Complaint also alleged that, during the time period of the antitrust conspiracy, Dwayne Andreas, ADM's Chairman and Chief Executive Officer, dominated and controlled the Board. Many ADM Board members were Andreas family members or friends, Company officers, close relatives of Company officers, or had ties with the Andreas family that raised serious questions as to whether the Board had performed its role properly or had been properly diligent. Plaintiffs alleged that these relationships made it highly unlikely that the Board would take effective action to investigate and remedy wrongdoing by Company executives. On October 17, 1995, plaintiff Deidra Graulich voluntarily dismissed the *Graulich* Action without prejudice.

16. Defendants moved to dismiss the First Consolidated Complaint or, in the alternative, to stay the action on October 31, 1995. On that same date, the United States District Court for the Northern District of Illinois ordered that the litigation, along with pending shareholder securities class actions, be transferred to the United States District Court for the Central District of Illinois. The litigation was subsequently transferred.

17. Defendants refiled their motion to dismiss or, in the alternative, to stay the action in the Central District Court on December 27, 1995. Defendants argued that plaintiffs had failed to make a demand upon the directors

of ADM as required by Delaware law before bringing their action, that plaintiffs failed to state a claim for relief against the defendants and that, Article XIV of ADM's Certificate of Incorporation shielded the defendants from liability for the misconduct plaintiffs alleged because it involved only a breach of their duty of care.

18. Shortly after the transfer order, plaintiffs served a document request on defendants. At a status hearing before the Court on February 26, 1996, the Court ruled that plaintiffs in the class and derivative shareholder actions were entitled to discovery of documents defendants had produced to the government or that the government had seized and that plaintiffs could request additional documents. Plaintiffs counsel reviewed and catalogued the tens of thousands of documents defendants produced but many categories of documents plaintiffs needed to prove their case were not produced. When plaintiffs sought additional limited discovery, defendants objected and filed a motion for a protective order to forestall any further discovery.

19. This litigation quickly focused on the issues defendants raised in their motions to dismiss and, in particular, whether plaintiffs were required to make demand on ADM's Board before bringing this action and whether defendants were shielded from liability under Delaware law because they had acted in good faith. Defendants' motions to dismiss the First Consolidated Complaint and for a protective order, both of which had been fully briefed, were set for hearing on April 26, 1996. At that hearing, the Court granted defendants' motion to dismiss without prejudice and gave plaintiffs leave to amend.

C. *The Consolidated and Amended Derivative Complaint.*

20. Plaintiffs filed a Consolidated and Amended Derivative Complaint (the "Complaint") on May 17, 1996.

By that time, Mark Whitacre had disclosed many of the details of the price-fixing activities in which he claimed that he and others at ADM had been involved. Whitacre disclosed meetings that he, Michael Andreas and Terrance Wilson attended with ADM's competitors in the lysine business where prices and market allocation were discussed. Whitacre stated publicly that illegal price-fixing was "fairly common" at ADM and had been going on since the early 1990's. Whitacre referred to comments made by the Company's President and its General Counsel, indicating that they were aware of price-fixing at the Company. Whitacre's accounts portrayed a corporation rife with criminal conduct at the highest levels and implicated one director, M.D. Andreas, directly and two others, Dwayne Andreas and James Randall, indirectly. Moreover, ADM continued to receive low marks from corporate governance experts and institutional shareholders, such as the California Public Employees' Retirement System ("CalPERS"), for its lack of both responsiveness to shareholders and Board independence.

21. The Complaint contained the results of counsel's review and analysis of the additional publicly available information on ADM and the Director Defendants. This case was unusual in that senior officials of the Company, with close ties to ADM's Board, were being investigated for criminal conduct and had exposed the Company to hundreds of millions of dollars in potential fines and damages. The Complaint incorporated this information in support of allegations that Michael Andreas, Dwayne Andreas and James Randall participated or assisted in the wrongdoing and that all directors were responsible for the wrongdoing at ADM because they had neither fulfilled their duties to prevent, detect and seek redress for criminal conduct nor exercised independent judgment in their oversight responsibilities.

22. With leave of the Court, plaintiffs filed a Supplement to the Complaint in November 1996 and an Amend-

ment and Supplement to the Complaint in December 1996. The Supplement updated the Complaint. The Amendment and Supplement to the Complaint alleged that the Director Defendants—other than Howard Buffett —had further breached their fiduciary oversight duties by failing to cause ADM to cooperate with the government in its investigation and minimalize criminal liability by demonstrating that ADM intended to remedy, prevent reoccurrence of, and seek redress for wrongdoing.

D. *Defendants' Further Motions to Dismiss and Objections to Discovery.*

23. Defendants moved to dismiss the Complaint on June 7, 1996. This motion was fully briefed. Defendants argued that plaintiffs had failed to make a pre-suit demand on ADM's Board of Directors as required by F. R. Civ. P. 23.1 and that demand was not excused in this case. Although agreeing that the relevant standard was whether the allegations of the complaint create a reasonable doubt that the Board could have exercised its independent and disinterested business judgment in responding to demand, the parties differed as to whether a majority of the Board could exercise such judgment.

24. Defendants also argued that the Complaint failed to state a claim for relief against 14 of the 17 Director Defendants because factual support necessary to show their misconduct was not alleged. In February, 1997, defendants filed a Supplemental Memorandum in Support of the Motion to Dismiss, arguing that plaintiffs' new allegations relating to the Board's failure to cooperate with the government should be dismissed because plaintiffs had failed to make demand on the Board and the new allegations failed to state a claim for relief. Defendants also argued that ADM's Certificate of Incorporation shielded the Director Defendants from liability for the new allegations as well.

25. While the motion to dismiss was pending, plaintiffs renewed their requests for documents. Defendants again objected to producing the requested documents because they had moved to dismiss the Complaint. Plaintiffs filed a motion to compel production of documents, and this motion was fully briefed.

26. The Court has not ruled on the motion to dismiss or the motion to compel and has adjourned argument on both motions pending the hearing on the Settlement.

27. In late October, 1996, plaintiffs sought discovery relating to ADM's wrongdoing from the Department of Justice, but the government refused to produce any of the evidence it possessed.

E. *ADM's Response to the Government's Investigation and Civil Litigation.*

28. After this lawsuit was commenced, ADM responded to charges of price-fixing in ADM products and criticism of its Board.

(a) ADM's Board appointed a Special Committee of outside directors to oversee the Company's response to the government's investigation and related civil litigation. In April, 1996, ADM announced that it had agreed to pay $25 million to settle the lysine civil antitrust case. On September 27, 1996, ADM announced that it had agreed to pay $35 million to settle the citric acid civil antitrust case. ADM also announced that it had agreed to pay $30 million to settle the federal securities class action brought by ADM stock purchasers.

(b) In October 1995, ADM's Board created the Corporate Governance Committee to review and make recommendations on corporate governance matters, such as Board structure and director qualifications. The Committee reported its recommendations to the Board on January 15, 1996. Subsequently, the Board reduced the number of directors, several directors, including Michael Andreas, did not stand for re-election, and the Board nominated three new outside directors for the 1996 term. Michael Andreas also took a leave of absence from the Company.

29. On October 15, 1996, ADM entered into a plea agreement with the United States Department of Justice in which ADM agreed to plead guilty and pay a $100 million criminal fine for fixing prices in the lysine market from June, 1992 through June 27, 1995 and for fixing prices in the citric acid market from January, 1993 through June 27, 1995. As part of the plea agreement, ADM agreed to cooperate with the government in current federal investigations of antitrust schemes. In return, the government agreed not to bring criminal charges against any current director, officer or employee of ADM (other than Michael D. Andreas and Terrance S. Wilson) for any antitrust violations covered in the ongoing investigations. There has been no evidence that any director of ADM, other than Michael Andreas, was aware of any price-fixing activities, or that the ADM Board systematically failed to exercise its oversight responsibilities.

III. SETTLEMENT NEGOTIATIONS AND THE SETTLEMENT

A. *Negotiation Of The Settlement And The Role Of Plaintiffs' Co-Lead Counsel In Implementing Corporate Governance Reforms At ADM.*

30. By the Fall of 1996, Plaintiffs' Co-Lead Counsel had concluded that ADM and its shareholders would be best served by a settlement that would change ADM's corporate governance and legal compliance rather than by protracted and uncertain litigation aimed at a monetary recovery for ADM. As of this time, the Company

had agreed to pay $190 million in criminal fines and in settlement of civil antitrust and securities class actions. ADM had made certain changes to the Board's membership after receiving the report of the Corporate Governance Committee. Plaintiffs' Co-Lead Counsel also recognized that, even if plaintiffs prevailed on the issue of demand futility—which was not certain—they would have difficulty demonstrating the defendants' willful or systematic failure to oversee the Company's operations necessary to establish liability under Delaware law. Moreover, Plaintiffs faced the likelihood the Company would create a special litigation committee to investigate director liability for the claims in this litigation—an action that would result in delay and could result in a decision to dismiss the litigation. Finally, Plaintiffs' Co-Lead Counsel took into account the primary interest of many ADM shareholders, including large institutional shareholders, which was to force changes in the way ADM's Board—and therefore ADM—functioned. With this background, Plaintiffs' Co-Lead Counsel contacted counsel for defendants and ADM in September 1996 to initiate settlement discussions. Plaintiffs' Co-Lead counsel were told that the defendants were not prepared to discuss settlement at that time.

31. After the Company entered into its plea agreement with the government and shortly before the November hearing on defendants' motion to dismiss and plaintiffs' motion to compel, defendants' counsel contacted Plaintiffs' Co-Lead Counsel to suggest continuing the hearing date to allow the parties to explore a possible settlement. Accordingly, Plaintiffs' Co-Lead Counsel began to prepare a settlement proposal to present to defendants. At the same time, however, Plaintiffs' Co-Lead Counsel pressed forward with the litigation and filed two additional pleadings.

32. At the outset, Plaintiffs' Co-Lead Counsel presented corporate governance measures that institutional

shareholders had requested and organizations and professionals who specialized in corporate governance had recommended, and other demands to ensure an environment at ADM that promoted Board independence and compliance with the law. Plaintiffs' Co-Lead Counsel were aware that, at ADM's October 1996 shareholder meeting, approximately 42% of ADM's shareholders had voted in favor of an amendment to ADM's by-laws to require a more restrictive definition of an outside director. ADM's Board had recommended a vote against the proposal. Also, 47% of the shareholders had voted in favor of a proposal requiring confidential voting, which ADM's Board also opposed. Both these proposals had been offered by large institutional shareholders. Although ADM's Board had nominated three new independent directors who were elected at the 1996 annual shareholders meeting, the Board had not implemented many of the recommendations of its Governance Committee; and ADM's Audit, Nominating and Compensation Committees were not comprised exclusively of outside directors.

33. Plaintiffs also sought a monetary contribution to the Company from the Director Defendants as part of the Settlement. Plaintiffs' Co-Lead Counsel received ADM's Directors and Officers Liability Insurance in effect when the litigation was commenced. The policy contained a $10 million policy limit and an exclusion for all claims, including derivative actions, arising from antitrust actions or proceedings.

34. Immediately prior to the December 11, 1996 hearing on pending motions, Plaintiffs' Co-Lead Counsel met with defendants' counsel to present plaintiffs' settlement demands. This framework Plaintiffs' Co-Lead Counsel established for a settlement was how best to strengthen the independence of the Board, prevent reoccurrence of the kind of problems ADM had experienced, and demonstrate to shareholders and the public that ADM was committed to good corporate governance. To this end, plaintiffs made a number of demands that included:

—Adopting the definition of outside director that 42% of ADM's shareholders had voted for;

—Establishing procedures for ensuring that future Board candidates were independent;

—Creating new Board Committees of outside directors with authority to investigate allegations of past misconduct, review current compliance and ensure future compliance with the law;

—Retaining outside independent counsel to assist these two new Committees;

—Requiring confidential voting;

—Retaining claims against Michael Andreas;

—The resignation of Dwayne Andreas as CEO and Chairman; and

—Some form of restitution to the Company by the Director Defendants for amounts expended to resolve criminal charges and civil litigation.

35. After two meetings in December 1996, one in Chicago and one in Washington, at which the parties negotiated plaintiffs' demands, plaintiffs submitted a written settlement proposal to defendants that contained the corporate governance measures presented and discussed at meetings between counsel, including the retention of independent counsel to assist Board Committees, a requirement that claims against Michael Andreas not be released and provision for some recoupment of monies to the Company, depending on the outcome of negotiations between defendants and the insurance carrier.

36. In connection with the negotiations, Plaintiffs' Co-Lead Counsel met separately with ADM's largest institutional shareholders, namely Kayla Gaylin, the general counsel of CalPERS, John Lukomnick, the Deputy Comptroller for Pensions of New York City, who has responsi-

bility for the City's pension fund investments, Bart Naylor of the Teamsters Pension Fund and Edward Durkin of the Carpenters Pension Fund, to solicit their views and review plaintiffs' proposals. In addition, Plaintiffs' Co-Lead Counsel spoke with Ann Hanson and Ann Yeager of the Council of Institutional Investors. These views, which primarily related to the definition of an outside director, were taken into account and, to the extent feasible, incorporated in plaintiffs' proposals. Plaintiffs' Co-Lead Counsel recognized that not all of these views could be implemented through the settlement of this litigation and continued to focus on institutionalizing measures and procedures that would provide the framework for an independent Board and an exemplary legal compliance program.

37. Throughout the negotiations, Plaintiffs' Co-Lead Counsel consulted with Professor John Coffee, Adolf A. Berle Professor of Law at Columbia University Law School, to make sure that the corporate governance measures being discussed were meaningful and of value to the Company. Plaintiffs' Co-Lead Counsel also consulted with R. Alan Miller, President of the Philadelphia Investment Banking Company, who provided an economic analysis of the settlement's value to ADM and its shareholders.

38. During negotiations, defendants' counsel reviewed with Plaintiffs' Co-Lead Counsel the in-depth and far-reaching study that ADM's Corporate Governance Committee had made of the current thinking on corporate governance before makings [*sic*] its recommendations to ADM's Board. For example, although Plaintiffs' Co-Lead Counsel believed the definitions of an outside director they proposed were more restrictive than those ADM's Governance Committee proposed, this was not always the case. After two further meetings, the parties reached an agreement on the definition of an outside director that took into account all parties' concerns and, significantly, defendants agreed to amend ADM's By-Laws to include

this definition and a statement of Board policies designed to ensure an independent Board.

39. As negotiations continued, plaintiffs also agreed to modify certain proposals, but the core demands remained intact. For example, plaintiffs insisted on restricting membership on the Audit and Nominating Committees to outside directors who had not been on the Board in June 1995, although this meant certain directors could not continue to serve on these Committees. The demand that claims the Company may have against Michael Andreas not be released raised further issues with the insurance carrier which was insisting that, if it acknowledged coverage, all defendants release any claims for further coverage in return for a payment on their behalf to settle this litigation.

40. Although ADM's counsel had declined a settlement proposal requiring Dwayne Andreas or any other individual defendant to resign, or the election to the Board of any particular individual, Plaintiffs' Co-Lead Counsel were advised that the Company would announce a significant change in Board structure and composition, consistent with plaintiffs' settlement demands for measures to create an independent Board, after the April 17, 1997 Board meeting. Indeed, on April 17, ADM announced that: Dwayne Andreas had retired as Chief Executive Officer of the Company; Lowell Andreas had retired from the Board; and former Ambassador Andrew Young had been elected to the Board. The Board also named G. Allen Andreas to be Chief Executive Officer and a member of the Board. These announcements complemented plaintiffs' settlement strategy of requiring ADM to implement structures and procedures for good corporate governance. Throughout the negotiations, defendants continued to update plaintiffs on the status of their negotiations wtih the insurance carrier over the coverage dispute. At the final stages of the negotiations between the parties, defendants advised plaintiffs that the carrier had finally agreed to pay $8 million on behalf of defendants.

41. After five months of arms-length negotiations between the parties, both face-to-face and by telephone, the parties agreed to a settlement that provided for corporate governance measures and procedures, the creation of a settlement fund of $8 million in cash to be paid into an interest bearing escrow account by the carrier, and the retention by the Company of any potential claims against Michael Andreas. On April 25, 1997, counsel for the parties began negotiations over the terms of a Memorandum of Understanding that would be the basis of a Stipulation of Settlement.

42. Even after the parties reached an agreement in principle, and they had agreed on the terms of the Memorandum of Understanding, they had to resolve how to dispose of a similar derivative action that was pending in Delaware. Because ADM's insurance carrier insisted on the dismissal of the Delaware action and ADM's directors insisted on a global settlement, Plaintiffs' Co-Lead Counsel sought to include the Delaware action in the Settlement. This required Plaintiffs' Co-Lead Counsel to meet with counsel for plaintiffs in the Delaware action and to hold further discussions with counsel for defendants and the Company. The result of these discussions was the change of a few words and the insertion of language into the corporate governance measures that reaffirmed that the Company has reporting and information systems in place. Finally, all parties executed the Memorandum of Understanding and entered into the Stipulation of Settlement on May 29, 1997.

43. Plaintiffs' Co-Lead Counsel drafted all of the Settlement papers during May 1997. After further discussions and revisions, including revisions to reflect that the Delaware action is to be dismissed upon this Court's approving the Stipulation of Settlement and entering a judgment, Plaintiffs' Co-Lead Counsel fiinalized the Stipulation of Settlement and exhibits.

B. *The Stipulation of Settlement.*

44. The Stipulation of Settlement negotiated by Plaintiffs' Co-Lead Counsel provides that the Board will adopt the following new corporate governance measures and procedures no later than 60 days after this Court's approval of the Settlement and the dismissals of this litigation and the Delaware action become final:

—a new definition of an outside director that will become part of ADM's By-Laws;

—a limit on the number of management directors, other than the Chief Executive Officer, to two ADM employees;

—a Nominating Committee comprised only of outside directors and, for the 1997 Board election, comprised exclusively of outside directors elected to the Board after the events that let [*sic*] to this lawsuit occurred;

—an outside director, either the Chairman if he qualifies or an elected Vice-Chairman, to preside over all meetings of non-management directors and the Governance Committee;

—an Audit Committee comprised only of outside directors and, for three years, comprised of outside directors who were elected to the Board after the events that led to this lawsuit occurred;

—a requirement that the Audit Committee engage outside independent counsel (to be paid from the settlement proceeds) for at least three years to advise it in connection with its oversight and legal compliance responsibilities, including determining whether the Company is violating any antitrust law, promulgating compliance policies and ensuring that employees adhere to these policies;

—a Governance Committee of non-management directors to assess Board and Committee effectiveness and evaluate the Chief Executive Officer;

—payment of at least one-half of director compensation in ADM stock with no increase in total compensation to a director for three years;

—confidential shareholder voting;

—a Public Policy Committee to promote communication between Company executives and investors, analysts, and other appropriate organizations.

45. The Settlement also requires the Director Defendants to pay, or to have paid in their behalf, $8 million (the "Settlement Proceeds") by June 2, 1997. This sum has been deposited in an interest-bearing account at Hickory Point Bank and Trust in Forsooth, Illinois. The Settlement Proceeds are to be used to pay reasonable attorneys' fees and expenses as ordered by the Court and the cost of Notice of the Settlement to current shareholders. The balance of the Settlement Proceeds will be paid to ADM to fund the expenses, costs and legal fees of the Audit Committee, for at least three years, to fulfill its independent review responsibilities, and for any training or educational efforts undertaken at the Audit Committee's direction.

46. The Settlement also provides that the plaintiffs will release defined claims against the Company and the Director Defendants and that the Company will release defined claims against the Director Defendants but will retain claims that it has against Whitacre and others, and that it may have against Michael Andreas and Terrance Wilson.

47. On May 30, 1997, this Court entered an Order preliminarily approving the terms of the Settlement and directing that Notice of the Settlement be provided to all current shareholders of ADM and that a summary notice of the proposed Settlement be pubilshed in *The Wall Street Journal.* Pursuant to this Order, over 243,000 Notices were mailed to ADM shareholders and the summary notice was published on June 13, 1997. The Affidavit of Publication is attached as Exhibit A.

C. *Evaluation Of The Proposed Settlement.*

48. Based on their factual and legal investigation of the claims and defenses in this litigation, the thorough briefing of two motions to dismiss, intense and protracted settlement negotiations, extensive consultation with experts and ADM's institutional investors, and their experience and familiarity with other similar actions, Plaintiffs' Co-Lead Counsel have concluded that the Settlement is fair, reasonable and adequate and in the best interests of ADM and its shareholders. The Settlement provides substantial benefits, a significant portion of which could not have been achieved through litigation, and avoids further, protracted, difficult and costly litigation with a risk of no recovery.

49. In analyzing the advantages and disadvantages of the settlement terms, Plaintiffs' Co-Lead Counsel at all times took into account the views and interests of ADM's shareholders, the benefit to the Corporation of the corporate governance measures, the interest of the Company in avoiding protracted and expensive litigation directed at ADM's past problems, and the risks of the litigation.

50. At the outset, plaintiffs had to overcome defendants' argument that plaintiffs cannot assert derivative claims because they failed to make pre-suit demand or demonstrate that demand was not required. Although plaintiffs believe they have a strong argument that a majority of ADM's Directors lacked the capacity to respond in good faith to a demand because they were interested in the litigation or were dominated by someone who had an interest, the outcome of this motion was not certain.

51. Once plaintiffs overcame this motion, they would face a number of obstacles in attempting to establish defendants' liability for the derivative claims. Defendants have argued that the conduct about which plaintiffs complain provides no basis for derivative liability because defendants acted reasonably and in good faith. Under

ADM's Certificate of Incorporation, directors are not liable for such conduct. Moreover, the claim that defendants failed to prevent wrongdoing by others is acknowledged to be a difficult claim on which to succeed. *In re Caremark International Inc. Derivative Litiga ion,* 1996 Del. Ch. LEXIS 125, 23, No. 13670 (Sept. 25, 1996). In order to prevail, plaintiffs would have to demonstrate intentional, reckless, or at least grossly negligent wrongdoing on the part of the directors. Plaintiffs would have to demonstrate the defendants' sustained or systematic failure to exercise oversight responsibilities. Defendants would contend that they had appropriate information gathering and reporting systems intact and that allegations of wrongdoing resulted from the misconduct of one employee, who was acting out of self-interest and who is not to be trusted.

52. Although ADM has been the subject of a federal criminal investigation and other civil litigation, none of these proceedings established findings or disclosed information that could be used to prove that the defendants in this action, other than Michael Andreas, breached their fiduciary duties to the Company. Plaintiffs also would have had difficulty in obtaining evidence to support their claims because most—if not all—fact witnesses would be defendants or ADM employees or agents.

53. Plaintiffs' Co-Lead Counsel took into account that the Company's director and officer liability insurance was limited and contained exclusions and that the Company could not reasonably expect to recover from the defendants anywhere near the more than $200 million that the antitrust violations had cost it. Therefore, a substantial monetary recovery was unlikely.

54. Based on these factors, Plaintiffs' Co-Lead Counsel have concluded that the Settlement is fair, reasonable and adequate and in the best interests of ADM and its shareholders.

IV. PLAINTIFFS' COUNSEL'S REQUEST FOR ATTORNEYS' FEES AND EXPENSES

55. Plaintiffs' counsel jointly request, as compensation for their substantial efforts and the results achieved, an aggregate fee award of $3,200,000, plus interest from June 2, 1997. Plaintiffs' counsel also seek $76,501.69 for reimbursement of expenses necessarily incurred in the prosecution of this litigation. The entire amount of this fee request is to be paid out of the Settlement Proceeds, the $8 million fund that the Director Defendants created to pay for corporate governance measures and attorneys' fees and expenses. No fees or expenses will be paid from ADM general corporate funds.

56. As noted, ADM's Corporate Governance Committee recommended a number of measures to ADM's Board in early 1996. At the time Plaintiffs' Co-Lead Counsel entered into negotiations with defendants' counsel, however, ADM had not adopted many of these measures. Based on shareholder demands and expert advice, plaintiffs insisted not only that ADM implement these measures, but also that ADM further tighten the qualifications for outside directors, amend its By-Laws to institutionalize the new definition of an outside director, and change the qualifications for membership on key Committees.

57. As part of the Settlement, ADM's Board agreed to adopt the corporate governance measures within 60 days. ADM's Board also agreed to a further restructuring of the Board and Committees that disqualified certain Director Defendants from continuing to serve on the Audit, Nominating and Compensation Committees, created the Corporate Governance Committee, required confidential shareholder voting and required that director compensation be paid partially in stock.

58. Moreover, ADM has agreed that a new Audit Committee, assisted by outside independent counsel to be

funded from Settlement Proceeds, will both (a) determine whether the Company is engaging in anti-competitive activities and (b) promulgate policies and procedures regarding compliance with all laws and the Company's procedures for educating employees and circulating these policies.

59. Plaintiffs' counsel's initiatives and perseverence were a substantial factor in ADM's adoption of the measures set forth in Exhibit A to the Stipulation of Settlement and were responsible for ADM's Board adopting and implementing these measures promptly.

60. Plaintiffs' counsel were aware in the early stages of settlement discussions that they might not be compensated even if they were successful in settling this litigation because of the limited amount of insurance coverage and the exclusion of coverage for antitrust-related litigation. Plaintiffs' counsel, however, did not allow this risk to impede their efforts to resolve this litigation for the benefit of ADM and its shareholders. It was only after Plaintiffs' counsel had spent months negotiating the settlement that they learned that the carrier had agreed to pay $8 million.

61. As set forth in the Miller Declaration, the economic value of this Settlement is $158 million. This value reflects the likelihood that the Settlement will avoid recurrence of the misconduct that led to this litigation, and its costs to ADM, and the effect the corporate governance measures have on ADM's market value. The total long-term economic value of this Settlement to ADM and its shareholders should be considered in determining the appropriate fee award in this case.

62. The notice mailed to ADM shareholders stated that the Company and the Director Defendants agreed not to oppose an application for an award of attorney fees and expenses up to 49% of the Settlement Proceeds. Only three objections to the fee request have been submitted.

63. Our firms, as *de facto* Plaintiffs' Co-Lead Counsel, were actively involved in all aspects of the prosecution of this action, and directed the work performed by the other plaintiffs' counsel after the cases were coordinated. Plaintiffs' counsel performed a wide range of services reflecting the complexity of the underlying facts and the difficult legal issues under Delaware law. The services our two firms performed included:

(a) Initial investigation and legal research concerning the merits of the case prior to filing the initial derivative complaints;

(b) Researching and drafting numerous pleadings, motions and memoranda, including:

(i) Proposed Consolidated and Amended Derivative Complaint;

(ii) Consolidated and Amended Complaint ("Complaint");

(iii) Supplement to Complaint;

(iv) Amendment and Supplement to Complaint;

(v) a memorandum in opposition to defendants' motion to dismiss or stay;

(vi) a memorandum in opposition to defendants second motion to dismiss;

(vii) a memorandum in opposition to defendants' motion for a protective order;

(viii) a Motion to Compel and supporting memoranda.

(c) Reviewing and analyzing ADM's public filings, press releases and documents produced to the government, ADM board minutes, ADM Corporate Governance Committee materials, and corporate governance treatises, articles and reports;

(d) Conferring over the course of the litigation with experts and institutional shareholders;

(e) Preparing for and appearing at all Court hearings in the United States District Courts for the Northern and Central Districts of Illinois;

(f) Conducting legal research and fact analysis;

(g) Preparing settlement proposals based on corporate governance measures and negotiating the Settlement;

(h) Drafting all settlement papers presented to the Court to effecuate the Settlement.

64. The lodestar of the firms which served as plaintiffs' counsel are detailed in the Appendix submitted herewith. The total lodestar of the seven firms is $1,257,320.75. The Appendix contains the sworn affidavits of each firm that served as plaintiffs' counsel, detailing the work they performed and their respective lodestars, based on each firm's current billing rates. Each firm's lodestar was prepared from contemporaneous, daily time records regularly prepared and maintained by that firm in the normal course of business.

65. Plaintiffs' Counsel also seek reimbursement of $76,501.69 in expenses which were necessarily incurred in the prosecution of this action. The expenses of Plaintiffs' Co-Lead Counsel included expert witness and consulting fees for plaintiffs' corporate governance and economics experts and travel expenses for meetings with ADM's institutional investors. These expenses are reflected on our firm's books and records. The expenses of the firms that served as Plaintiffs' counsel are detailed in sworn affidavits contained in the Appendix submitted herewith.

66. As set forth in detail above, plaintiffs' counsel faced tremendous risks in pursuing this litigation. Recovery was not assured. ADM's limited insurance coverage with its antitrust exclusions increased the risk that there

would be no compensation. Moreover, Plaintiffs' counsel have received no compensation during the course of this litigation, their fees being totally contingent and dependent upon a successful result.

67. Plaintiffs' counsel achieved this outstanding Settlement quickly and efficiently, without unnecessary attorney time and expense.

68. Plaintiffs' counsel are requesting attorneys' fees of $3,200,000, plus interest, an amount that is forty percent (40%) of the Settlement Proceeds and less than the Company and the defendants have agreed not to oppose. We respectfully submit that Plaintiffs' counsel's fee request is fair, reasonable and justified and that the Court should grant Plaintiffs' counsel's joint application for an award of attorneys' fees and expenses.

V. OBJECTIONS TO THE SETTLEMENT

69. Two objections to the settlement have been filed, and three individual shareholders have objected—one in a letter to the Court—to an award of fees and expenses to plaintiffs' counsel of 49% of the Settlement Proceeds. The Notice advised shareholders that the Director Defendants and the Company agreed not to oppose applications for fees and expenses that did not exceed 49% of the Settlement Proceeds ($3,920,000).

70. One objection to the Settlement has been made by John J. Gilbert and Martin Glotzer because the Settlement does not require that ADM adopt cumulative voting. These objectors do not explain why cumulative voting should be part of this settlement. In fact, this objection suggests a change that is inconsistent with the Settlement's objective of strengthening Board independence and having directors who will serve in the best interests of all shareholders. This objection should be denied.

71. The second objection to the Settlement has been filed by Charles W. Pauly. Mr. Pauly contends that the

plaintiffs should be required to try their case because, if the claims have merit, the Settlement is inadequate, and if the case is without merit, the case should not be settled. Mr. Pauly not only overlooks the substantial non-monetary benefits from the Settlement, but he also fails to appreciate that plaintiffs would be unlikely to recover large sums of money from the Director Defendants even if they prevailed. He also apparently does not understand that this litigation was brought on behalf of ADM and that ADM is benefitting from the Settlement fund, not contributing to it. This objection should be denied.

72. The three shareholders who object to fees, Mitchell Berns, John P. Chiara, and Peter D. Scott, state that they believe 49% is too high a percentage. All three objectors focus only on the $8 million fund and do not consider that the value of the Settlement is much greater, that ADM is not contributing to the fund but rather will be receiving more than half of it, and that plaintiffs' efforts caused the fund to be created. The Director Defendants and the Company agreed that reasonable attorneys' fees and expenses should be paid from the Settlement Proceeds and that an award of 49% ($3,920,000 plus interest) was acceptable to them. Plaintiffs' counsel are requesting a fee of $3,200,000, plus interest, which represents 40% of the Settlement Proceeds, plus their expenses, which is less than the Director Defendants and the Company agreed not to oppose. In a letter to the Court, Mr. Chiara suggests further that there may be a conflict between plaintiffs and their counsel because the defendants do not object to the fee. In this case, however, there is no conflict because Plaintiffs' counsel's fees are not paid from any recovery that would otherwise go to the individual plaintiffs. Further, the Company is represented by independent counsel, who have reviewed the fairness to ADM of all the terms of the Settlement, including the agreement not to oppose an award of fees and expenses of up to $3,920,000. These objections should be denied.

CONCLUSION

73. Plaintiffs' Counsel believe that the Settlement, which will promptly bring about significant and highly valuable corporate governance reforms for the benefit of ADM and its current and future shareholders, is far more beneficial than continuing to litigate for an uncertain outcome and the possibility of no recovery for ADM. Plaintiffs' Counsel believe that the proposed Settlement is fair, reasonable, and adequate and should be approved, along with plaintiffs' counsel's request for an award of attorneys' fees and expenses.

We jointly declare under penalty of perjury that the foregoing is true and correct and that this Declaration is executed this 30 day of June, 1997.

/s/ Terry Rose Saunders
TERRY ROSE SAUNDERS

/s/ Robert M. Roseman
ROBERT M. ROSEMAN

EXHIBIT A

STATE OF MASSACHUSETTS)
COUNTY OF HAMPDEN) ss:
CITY OF CHICOPEE)

I, MARGARET YERGEAU, being duly sworn, depose and say that I am the Advertising Clerk of the Publisher of *THE WALL STREET JOURNAL*, a daily national newspaper published and of general circulation in the City and County of New York, in the City of Naperville, DuPage County, Illinois, and in the City and County of Dallas, Texas, and that the attached Notice has been regularly published in *THE WALL STREET JOURNAL* for national distribution for ONE (1) insertion(s) on the follofing date(s): JUNE 13, 1997 and that the foregoing statements are true and correct to the best of my knowledge, information and belief.

/s/ Margaret S. Yergeau

[Notary Omitted in Printing]

IN THE UNITED STATES DISTRCT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

[Caption Omitted in Printing]

AFFIDAVIT OF JOHN C. COFFEE, JR.

John C. Coffee, Jr., being duly sworn, deposes and says:

1. I am the Adolf A. Berle Professor of Law at Columbia Univerity Law School and have taught corporate and securities law for over twenty years (at Columbia and at the law schools of Stanford University, the University of Michigan, the University of Virginia and Georgetown University). Prior to that, I was a practicing corporate lawyer with the firm of Cravath, Swaine & Moore in New York City from 1970 to 1976.

2. As a law professor, one of my principal areas of specialization has been the field of corporate governance. I am a member both of the Legal Advisory Committee to the Board of Directors of the New York Stock Exchange, Inc. and of the Legal Advisory Board of the National Association of Securities Dealers ("NASD"). I served (for over a dozen years) as a Reporter to the American Law Institute for its restatement on corporate fiduciary duties: See A.L.I., PRINCIPLES OF CORPORATE GOVERNANCE: Analysis and Recommedations (1992) (hereinafter, "ALI Principles"). I am also a co-author of Choper, Coffee and Gilson CASES AND MATERIALS ON CORPORATIONS (3rd ed. 1995); Jennings, Marsh & Coffee, CASES AND MATERIALS ON SECURITIES REGULATION (4th ed. 1992), and Klein

and Coffee, BUSINESS ORGANIZATION AND FINANCE: Legal and Economic Principles (5th ed. 1993), all widely used law school casebooks or textbooks that cover the subject matter of corporate governance. Finally, I have also recently served as a member of the SEC's Advisory Committee on the Capital Formation and Regulatory Processes, am a member of the Executive Committee of the Securities Regulation Institute, and write a regular column on corporate and securities law for both the New York Law Jouranl and the Natonal Law Journal. A fuller listing of my activities and writing is set forth on my resume, which is attached hereto as Exhibit A.

3. Another area in which I have specialized and which is applicable to this case is that of "white collar crime", with a special focus on organizational misconduct. In that regard, I have served as a consultant to the United States Sentencing Commission in connection with its formulation of sentencing guidelines for organizational offenders and served as a Reporter to the American Bar Association for its Standards on Sentencing Alternatives and Procedures (which standards covered organizational sentencing).

4. In this action, I have been retained by the plaintiffs' attorneys to appraise the adequacy and significance of the corporate governance provisions set forth in Exhibit A to the Stipulation of Settlement, dated May 29, 1997 (hereinafter, the "Corporate Governance Provisions"). In considering these provisions, I have compared them with (1) the standards set forth in the ALI Principles; (2) the Corporate Directors' Handbook (the "Handbook") prepared by the Business Law Section of the American Bar Association;[1] (3) certain statements of the Council of Institutional Investors, including its Shareholder Bill of Rights and its definition of "independ-

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[1] See Section on Business Law, *Corporate Directors' Handbook*, 49 Bus. Law. 1243 (1994).

ent director;"[2] (4) certain proposed guidelines drafted by Calpers, the nation's largest public pension fund,[3] (5) the guidelines of the National Association of Corporate Directors;[4] and (6) the 1994 General Motors Guidelines on Significant Corporate Governance Issues (hereinafter, the "GM Guidelines").[5] Both the Handbook and the GM Guidelines have been described as "very helpful" by the Chief Justice of the Delaware Supreme Court in determining director independence and "aspirational corporate practices," and he has recommended that they "should be consulted by boards and their advisers."[6]

5. In general, I believe the Corporate Governance Provisions represent more or less the "state of the art" in American corporate governance today. This is not to say that every conceivable reform provision has been adopted, but virtually every reform about whose desirability there today exists a significant consensus among commentators and institutional investors has been incorporated. In addition, beyond these corporate governance provisions, there are special legal compliance provisions that I believe are of special value to a corporation with Archer Daniels Midland's ("ADM") history. In this affidavit, I undertake to review these separate provisions, first individually and then in terms of their aggregate impact.

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[2] This statement is attached hereto as Exhibit B.

[3] See Adam Bryant, "Calpers Draws a Blueprint for Its Concept of An Ideal Board", New York Times, June 17, 1997 at D-1.

[4] See John A. Byrne, "The National Association of Corporate Directors' new guidelines won't tolerate inattentive, passive uninformed board members," Business Week, November 25, 1996 at p. 100.

[5] See General Motors Guidelines, reprinted in Corporate Governance Advisor, May-June, 1994, at 3-4.

[6] See E. Norman Veasey, *The Defining Tension in Corporate Governance in America*, 52 Bus. Law. 393, 399 (1997).

I. *Corporate Governance Provisions*

6. Initially, the Corporate Governance Provisions require that "a majority of the Board shall be comprised of outside directors." (See Section I "Board Structure and Policies"). This is the norm today for publicly traded companies and does not in itself reflect any significant step forward. However, this same section goes on to provide that direct management representation on the board "should be kept to a minimum and should in no event exceed two other management directors." Although this is again in keeping with current practice, this express limitation is relatively rare. The recently released Korn/Ferry's 24th Annual Board of Directors Study finds that the typical public board today has eleven members, only two of whom are insiders.[7] The formal recognition of a principle that the management directors should be limited to a maximum of three has positive value and is thus an advance over current prevailing practice. Because this provision will be incorporated into ADM's bylaws and cannot be repealed without specific disclosure and an SEC filing, there is considerable reason to believe it will be a permanent feature of ADM's future corporate governance.

7. More importantly, the definition of "outside director" in the Corporate Governance Provisions is tighter and more restrictive than those set forth in most of the well-known contemporary corporate governance guidelines. Its definition appears to be modeled after the Council of Institutional Investors' "Definition of an Independent Director" (attached hereto as Exhibit B). I believe this definition is particularly meaningful and relevant to ADM's case because it will effectively preclude the counting of business consultants or advisers to ADM as outside directors.

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[7] See "Cash Compensation Drops for Outside Directors, annual Korn/Ferry Study Reveals," Business Wire, May 7, 1997.

8. The Corporate Governance Provisions also effectively endorse the "lead director" concept. This idea emanates from an important article by Jay Lorsch and Martin Lipton,[7] which recommended the appointment of a "lead director" to oversee the functioning of the board. Effectively, the existence of formally designated lead director creates a safety valve or check within the board on the influence of a dominating CEO, and it does so without requiring the automatic separation of the CEO and Chairman positions (which some feel can compromise the authority of the CEO and result in inefficiency). The GM Guidelines effectively endorsed this principle. Here, the "lead director" will in effect be either the Chairman (if the Chairman is an outside director) or the Vice-Chairman (if not) (See Section IV ("Leadership of the Board").

9. While highly meritorious in my judgment, the "lead director" concept remains controversial. A 1996 survey of board practices finds that 79% of respondents opposed designating a "lead director" for their board.[8] In that light, the Corporate Governance Provisions take an important, but still novel, step toward establishing a board capable of withstanding managerial pressures. The Corporate Governance Provisions cannot thus be criticized for simply adopting a widely prevalent model for corporate governance; rather they impose on the board controls and procedures that are resisted by most corporate executives today and would not be likely to have been adopted, absent the current litigation.

10. Another important innovation is the Governance Committee (See "Section IV Governance Committee").

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[7] See Martin Lipton & Jay W. Lorsch, *A Modest Proposed* [*sic*] *for Improved Corporate Governance* 48 Bus. Law. 59 (1992); see also, Jay W. Lorsch & Martin Lipton, *On the Leading Edge: The Lead Director Concept*, Harv. Bus. Rev., Jan.-Feb., 1993 at 79.

[8] See the IRCC Monitor: Board Practices Survey, Corporate Governance Advisor, May/June 1996 at 25-26.

The critical idea underlying this committee is the need for an at least annual review of the board's performance and that of the Chief Executive Officer (in the latter case the review is to be by all nonmanagement directors). Again this requirement is consistent with the philosophy and approach of the GM Guidelines, and it is to be backstopped and enforced by annual disclosures about "the performance criteria and evaluation process in the Company's proxy statement." Because the idea of an annual board review of the CEO's performance has been widely resisted by corporate executives,[9] its adoption seems unlikely, but for this litigation.

11. Other meaningful changes introduced by the Corporate Governance Provisions include the adoption of confidential voting and the addition of new outside directors to both the Audit and Nominating Committees. As a result of these changes, no member of management will continue on the Nominating Committee under the Corporate Governance Provisions.

12. Collectively, the combination of the lead director provision, the annual board review, and the requirements that (a) the Audit Committee be composed "solely of outside directors" for the next three years (see "Section V. Independent Review Responsibilities of the Audit Committee") and (b) the Nominating Committee for the 1997 board election be composed "of outside directors who were first elected to the Board of Directors after June 25, 1996," represent in my judgment significant steps to facilitate board independence and to end the apparent managerial domination of the ADM board. Although it is never possible to predict that these changes will of necessity be succesful, there is frankly little more than [*sic*] can be done from a corporate governance perspective in terms of board structure or procedures.

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[9] In the same IRRC survey discussed above, 62.9% of respondents disfavored any policy whereby outside directors would hold periodic meetings without the presence of the CEO. *Id.* at 25-26.

II. *Law Compliance*

13. ADM is incorporated in Delaware, and under Delaware corporate law the ADM board of directors owes a duty of care to ADM under which it must supervise and monitor the corporation's performance, including for possible violations of law. See, *In re Caremark International Inc. Derivative Litigation,* 1996 Del. Ch. LEXIS 125 (Del. Ch. Sept. 25, 1996).

14. The Corporate Governance Provisions take important steps in addressing and rectifying any legal compliance deficiencies by expressly assigning to ADM's Audit Committee new oversight responsibilities for law compliance, including issues of antitrust, discrimination, foreign corrupt practices act enforcement, environmental conduct and federal securities laws requirements. This assignment is not simply a general precatory instruction, but rather an order (a) to determine whether ADM is engaged in anti-competitive activities and (b) to promulgate policies and procedures regarding (i) compliance with the law, (ii) ADM's procedures for educating employees about compliance with the law; and (iii) ADM's procedures for circulating these policies. The Audit Committee is further charged with authority to ensure adherence to these policies and procedures. Additional specific instructions require:

(1) the retention of outside independent counsel (for at least a three year period) to advise and assist the Audit Committee;

(2) the appointment to the Audit Committee of only outside directors, and, for three years, only outside directors who were first elected to the board after June 25, 1995.

15. It is important to recognize that, to the extent these requirements introduce new compliance policies and procedures by newly appointed Committee members and

advisers, they will help guard against the significant financial liability that could result from having corporate officers violate the federal criminal and civil laws in the future.[10] Thus, there is a corporate benefit from the installation of these new oversight responsibilities.

CONCLUSION

16. Ultimately, it is impossible to predict that ADM will not violate the law again. No system of safeguards is foolproof; nor can every contingency be anticipated. But the Corporate Governance Provisions do that which can feasibly be done: establish a framework for effective monitoring and facilitate the evolution (which will not necessarily occur overnight) of an active and independent board. Such therapeutics have value (as the United States Sentencing Commission has independently determined). Indeed, so long as the board structure contemplated by the Corporate Governance Provisions is not modified or abridged, I believe that it is a prudent prediction that ADM will soon have an effective and independent board that will engage in active monitoring.

/s/ John C. Coffee, Jr.
JOHN C. COFFEE, JR.

[Notarization dated 25 June 1997 Omitted in Printing]

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[10] In 1991, pursuant to the Sentencing Reform Act of 1994, the United States, Sentencing Commission adopted Organizational Sentencing Guidelines, which greatly enhanced the criminal fines (and other sanctions) for corporate and other organizational defendants in federal court, but also offered a correspondingly substantial credit against these presumptive sentences for organizations that adopted an "effective program to prevent and detect violations of law." See United States Sentencing Commission, Guidelines Manual, Chapter 8, § 8A1.2, Application Note 3(k) (defining such an "effective program"). This affiant was a consultant to the Commission in this process.

EXHIBIT A

RESUME

John Collins Coffee, Jr.
320 Wyoming Avenue
Maplewood, New Jersey 07040

POSITION:

Adolf A. Berle Professor of Law, Columbia University Law School

EDUCATION:

Amherst College 1966 B.A. (*magna cum laude*) Bond Fifteen (highest fifteen ranking seniors); Phi Beta Kappa

LAW SCHOOLS:

Yale Law School 1969, LL.B; New York University Law School, 1976 LL.M (in Taxation).

OCCUPATIONAL HISTORY:

Columbia Law School 1980--present; Berle Chair since 1986

Stanford Law School—Visiting Professor, Spring 1987

Virginia Law School—Visiting Professor, Fall 1979

Michigan Law School—Visiting Professor, Summer 1979

Georgetown University Law School—Professor and Associate Professor, 1976-1980

Cravath, Swaine and Moore—Associate, 1970-1976
Reginald Heber Smith Fellowship, 1969-1970

SPECIALIZATIONS:

My academic teaching specialties include corporate and securities law, class actions and complex litigation, criminal law, and white collar crime.

OTHER ACTIVITIES and HONORS:

1. Fellow, American Academy of Arts and Sciences
2. Reporter (for Litigation Remedies), American Law Institute, PRINCIPLES OF CORPORATE GOVERNANCE AND STRUCTURE (1980-1993: Final Draft 1993)
3. Reporter, American Bar Association, MINIMUM STANDARDS FOR CRIMINAL JUSTICE (2nd ed. 1980)
4. Member, Advisory Committee on Capital Formation and Regulatory
5. Member, Legal Advisory Committee to the Board of Directors, New York Stock Exchange (1992-1995) (currently, emeritus member)
6. Member, Legal Advisory Board, National Association of Securities Dealers (NASD) (1996-)
7. Member, Market Practices Committee, NASD Regulation, Inc. (1997-)
8. Member, Subcouncil on Capital Allocation, United States Competitiveness Policy Council (created by Omnibus Trade and Competitiveness Act of 1988) (1993-1995)
9. Member, Standing Committee on Law and Justice, Commission on Behavioral and Social Sciences and Education, National Research Council (elected to 1990-1994 term)

10. Member, National Academy of Sciences Panel on Research on Sentencing (1979-1982)
11. General Counsel, American Economic Association (1992-)
12. Fellow, American Bar Foundation
13. Member, American Law Institute
14. Chairperson, Section on Business Associations, Association of American Law Schools (AALS) (1981-1982)
15. Chairperson, Audit and Investment Policy Committee, AALS (1992-1994) and former member, Nominating Committee, AALS (1990-1991)
16. Chairperson, Committee on Sections, AALS (1984-1985)
17. Board of Editors, M&A and Corporate Governance Law Reporter
18. Board of Contributing Editors, American Lawyer Newspaper Group
19. Columnist on Corporate and Securities Law, New York Law Journal
20. Businesswatch Columnist, National Law Journal
21. Member, Special Committee on Mergers, Acquisitions and Corporate Control, Contests (1996-), and former member, Committee on Corporate Laws (1994-1995), Committee on Securities Regulation (1991-1994) and Committee on Corporate Laws (1983-1985), Association of the Bar of the City of New York
22. Member, Executive Committee, Securities Regulation Institute (1992-1996)
23. Chairperson, Appointments Committee, Columbia Law School (1987-1990)

24. Frequent Panelist at PLI, ALI-ABA, SEC and other Seminars and Institutes and have testified before Congress.

BOOKS, AND CASEBOOKS

1. Choper, Coffee and Gilson, CASES AND MATERIALS ON CORPORATIONS, (Little Brown & Co.) (4th edition 1985)
2. Jennings, Marsh, and Coffee, CASES AND MATERIALS ON SECURITIES REGULATION (7th ed. 1992)
3. Reporter, ABA MINIMUM STANDARDS FOR CRIMINAL JUSTICE (2d ed. 1980) (Chapter 18)
4. Klein and Coffee, BUSINESS ORGANIZATION AND FINANCE (6th ed. 1996)
5. Coffee, Lowenstein and Rose-Ackerman, KNIGHTS RAIDERS AND TARGETS: The Impact of The Hostile Takeover (Oxford University Press, 1988)
6. Tonry and Zimring, REFORM AND PUNISHMENT (Chicago University Press 1984) (one third of this book is an essay by Coffee)

LAW REVIEW ARTICLES: (in reverse chronological order)

1. Coffee, *Transfers of Corporate Control and the Triggering Thesis: Can Delaware Law Encourage Efficient Transactions While Chilling Inefficient Ones?*, 21 Del. J. Corp. L. 359 (1996).
2. ———, *The Future of the Private Securities Litigation Reform Act of 1995: or Why the Fat Lady Has Not Yet Sung*, 51 Bus. Law. 975 (1996).

3. ———, *Class Wars: The Dilemma of the Mass Tort Class Action*, 95 Colum. L. Rev. 1343 (1995).

4. ———, *Competition versus Consolidation: The Significance of Organizational Structure in Financial and Securities Regulation*, 50 Bus. Law. 447 (1995)

5. ———, *Hail Britannia?: Institutional Investor Behavior Under Limited Regulation*, 92 Mich. L. Rev. 1997 (1994) (with Black)

6. Coffee, *The SEC and the Institutional Investor: A Half-Time Report*, 15 Cardozo Law Review 837 (1994)

7. ———, *New Myths and Old Realities: The American Law Institute Faces the Derivative Action*, 48 Bus. Law. 1407 (1993)

8. ———, *Paradigms Lost: The Blurring of the Criminal and Civil Law Models—And What Can Be Done About It*, 101 Yale L.J. 1875 (1992)

9. ———, *Liquidity Versus Control: The Institutional Investor as Corporate Monitor*, 91 Colum. L. Rev. 1277 (1991)

10. Coffee and Klein, *Bondholder Coercion: The Problem of Constrained Choice in Debt Tender Offers and Recapitalizations*, 58 U. Chi. L. Rev. 1207 (1991)

11. Coffee, *Does "Unlawful" Mean "Criminal"? Reflections on the Disappearing Tort/Crime Distinction in American Law*, 71 B.U.L. Rev. 193 (1991)

12. ———, *Unstable Coalitions: Corporate Governance as a Multi-Player Game*, 78 Geo. L.J. 1495 (1990)

13. ———, *The Mandatory/Enabling Balance in Corporate Law: An Essay on the Judicial Role*, 89 Columbia. L. Rev. 1618 (1989)

14. ———, Hush!: *The Criminal Law Status of Confidential Business Information After McNally and Carpenter and the Enduring Problem of Overcriminalization*, 26 Amer. Crim. L. Rev. 121 (1989)

15. ———, *The Uncertain Case for Takeover Reform: An Essay on Stockholders Stakeholders and Bust-ups*, 1988 Wisc. L. Rev. 435

16. ———, *The Regulation of Entrepreneurial Litigation: Balancing Fairness and Efficiency in the Large Class Action*, 54 U. Chi. L. Rev. 877 (1987)

17. ———, *Rethinking the Class Action: A Policy Primer on Reform*, 62 Ind. L. Rev. 625 (1987)

18. ———, *Shareholders Versus Managers: The Strain in the Corporate Web*, 85 Michigan L. Rev. 1 (1986)

19. ———, *Understanding the Plaintiff's Attorney: The Implications of Economic Theory for Private Enforcement of Law Through Class and Derivative Actions*, 86 Colum. L. Rev. 669 (1986)

20. ———, *The Future of Corporate Federalism*, 8 Cardozo L. Rev. 759 (1987)

21. ———, *The Unfaithful Champion: The Plaintiff as Monitor in Shareholder Litigation*, 48 Law and Contemporary Problems 5 (1985)

22. ———, *Partial Justice: Balancing Fairness and Efficiency in Partial Bids*, 3 Companies and Securities Law Review 216 (Australian Law Review).

23. ———, *Litigation and Corporate Governance: An Essay on Steering Between Scylla and Charybdis*, 52 Geo. Wash. L. Rev. 789 (1985)

24. ———, *Market Failure and the Economic Case for a Mandatory Disclosure System*, 70 Va. L. Rev. 717 (1984)

25. ———, *Regulating the Market for Corporate Control: A Critical Assessment of the Tender Offer's Role in Corporate Governance*, 84 Colum. L. Rev. 1145 (1984)

26. ———, *Rescuing the Private Attorney General: Why the Model of the Lawyer As Bounty Hunter is Not Working*, 42 Maryland Law Review 215 (1983)

27. Coffee and Schwartz, *The Survival of the Derivative Suit: An Evaluation and a Proposal Legislative Reform*, 81 Colum. L. Rev. 261 (1981)

28. Coffee, *"No Soul To Damn; No Body Kick," An Unscandalized Inquiry into the Problem of Corporate Punishment*, 79 Mich. L. Rev. 386 (1981)

29. ———, *"Twisting Slowly In the Wind": A Search for Constitutional Limits on Coercion of the Criminal Defendant*, 1980 Supreme Court Review 211 (1981)

30. *Beyond the Shut-Eyed Sentry: Toward a Theoretical View of Corporate Misconduct and an Effective Legal Response*, 62 Va. L. Rev. 1099 (1977)

31. ———, *The Repressed Issues in Sentencing: Accountability, Predictability and Equality in the Era of the Sentencing Commission*, 66 Geo. L.J. 975 (1978)

32. ———, *The Future of Sentencing Reform*, 73 Mich. L. Rev. 1361 (1975)

33. ———, *Making the Punishment Fit the Corporation: The Problems of Finding an Optimal Corporate Criminal Sanction*, 1 N. Ill. L. Rev. 1 (1980)

34. ———, *Privacy versus Parens Patriae*, 57 Cornell L. Review 571 (1972)

ENDOWED LECTURES

Professor Coffee has delivered annual endowed lectures at the American University, the University of Arizona, Cleveland-Marshall Law School, the University of Colorado, Delaware Law School, the Marshall-Wythe Law School of the College of William and Mary, the University of Maryland, and Washington and Lee University, served as a Distinguished Visiting Scholar at the University of Toronto Law School and Osgoode Hall Law School, and taught as a visiting scholar at the University of Tokyo. He has also given numerous faculty workshops at other law schools.

EXHIBIT B

COUNCIL OF
INSTITUTIONAL
INVESTORS

Suite 512 • 1730 Rhode Island Avenue, N.W.
Washington, D.C. 20036
(202) 822-0800 • Fax (202) 822-0801

COUNCIL OF INSTITUTIONAL INVESTORS

DEFINITION OF INDEPENDENT DIRECTOR

An independent director is someone whose only non-trivial connection to the corporation is that person's directorship.

A director will not generally be considered independent if he or she:

(a) has been employed by the corporation or an affiliate in an executive capacity;

(b) is an employee or owner of a firm that is one of the corporation's or its affiliate's paid advisers or consultants;

(c) is employed by a significant customer or supplier;

(d) has a personal services contract with the corporation or one of its affiliates;

(e) is employed by a foundation or university that receives significant grants or endowments from the corporation or one of its affiliates;

(f) is a relative of an executive of the corporation or one of its affiliates;

(g) is part of an interlocking directorate in which the CEO or other executive officer of the corporation serves on the board of another corporation that employs the director.

EXPLANATORY NOTES

An independent director is someone whose only non-trivial connection to the corporation is that person's directorship.

NOTES: Independent directors do not invariably share a single set of qualities that are not shared by non-independent directors. Consequently, no clear rule can unerringly describe and distinguish independent directors. However, members of the Council of Institutional Investors believe that the promulgation of a narrowly drawn definition of an independent director (coupled with a policy specifying that a majority of board members should meet this standard), is in the corporation's and all shareholders' on-going financial interest because:

—a genuine quality of independence is critical to a properly functioning board,

—certain clearly definable relationships pose a sufficient threat to a director's unqualified independence in a sufficient number of cases that they warrant advance identification,

—the effect created by a conflict of interest on an individual director is almost impossible to detect, either by shareholders or other board members, and,

—while an across-the-board application of *any* definition to a large number of people will inevitably miscategorize a few of them, this is sufficiently small that it is far outweighted by the significant benefits.

Stated most simply, an independent director is a person whose directorship constitutes his or her only connection to the corporation. The definition approved by members of the Council contains this basic formulation. It then adds to it a list of the relationships members believe pose the greatest threat to a director's independence. The existence of any such relationship will remove a director from the independent category. Relationships not described in this list will not be considered in assessing independence.

The following notes are supplied to give added clarity and guidance in interpreting the specified relationship.

(a) has been employed by the corporation or an affiliate in an executive capacity

NOTES: The term "executive capacity" includes the chief executive, operating, financial, legal, and accounting officers of a company. This includes the president, treasurer, secretary, controller, and any vice-president who is in charge of a principal business unit, division, or function (such as sales, administration, or finance) or performs a major policymaking function for the corporation.

An "affiliate" relationship is established if one entity either alone or pursuant to an arrangement with one or more other persons, owns or has the power to vote more than 25 percent of the equity interest in another, unless some other person, either alone or pursuant to an arrangement with one or more other persons, owns or has the power to vote a greater percentage of the equity interest. For these purposes, equal joint venture partners meet the definition of an affiliate, and officers and employees of equal joint venture enterprises are considered affiliated.

Affiliates include predecessor companies. A "predecessor" of the corporation is a corporation that within the last ten years represented more than 80 percent of the corporation's sales or assets when such predecessor became part of the corporation. Recent merger partners are also considered predecessors. A recent merger partner is a corporation that directly or indirectly became part of the corporation or a predecessor within the last ten years and represented more than 50 percent of the corporation's or predecessor's sales or assets at the time of the merger.

A subsidiary is an affiliate if it is at least 80% owned by the corporation and accounts for 25% of the corporation's consolidated sales or assets.

(b) is an employee or owner of a firm that is one of the corporation's or its affiliates paid advisers or consultants;

NOTES: Advisors or consultants include, but are not limited to, law firms, accountants, insurance companies, and banks.

(c) is employed by a significant customer or supplier;

NOTES: A director shall be deemed to be employed by a significant customer or supplier if the director:

—is employed by or has a 5 percent or greater ownership interest in a supplier or customer where the sales to or by the corporation represent more than 1% of the sales of the customer or supplier or for more than 1% of the sales of the corporation,

—is employed by or has a 5 percent or greater ownership interest in one of the corporation's debtors or creditors where the amount owed exceeds 1% of the corporation's or the third party's assets.

Ownership means beneficial or record ownership, not custodial ownership.

(d) has a personal services contract with the corporation or one of its affiliates;

NOTES: The Council members believe that even small personal services contracts, no matter how formulated, can threaten a director's complete independence. This includes any arrangement under which the director borrows or lends money to the corporation at rates better (for the director) than those available to normal customers—even if no other services from the director are specified in connection with this relationship.

(e) is employed by a foundation or university that receives significant grants or endowments from the corporation or one of its affiliates;

NOTES: This relationship includes that of any director who is a salaried executive of a non-profit organization to which the corporation or its affiliate gives more than $100,000 or 1% of total annual donations received (whichever is less), or who is a *direct* beneficiary of *any* donations to such an organization.

(f) is a relative of an executive of the corporation or one of its affiliates;

NOTES: Relatives include spouses, parents, children, siblings, mothers and fathers-in-law, sons and daughters-in-law, brothers and sisters-in-law, aunts, uncles, nieces, nephews, and first cousins. Executives include those serving in an "executive capacity."

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA DIVISION

[Caption Omitted in Printing]

DECLARATION OF R. ALAN MILLER

I, R. Alan Miller, declare as follows:

Qualifications

1. I am President of Philadelphia Investment Banking Company. My resume is attached as Exhibit A hereto to describe my educational background and experience.

2. Philadelphia Investment Banking Company ("PIBC") provides a wide range of corporate finance services to clients. These services include raising capital through private placements of debt and equity financings; financial analysis and advisory services re: public offerings of securities; merger, acquisition and divestiture services; evaluation and economic analysis services; consulting and litigation support; and other financial services.

3. PIBC and its principals perform a considerable amount of work in the areas of evaluation of businesses and securities and the factors involved in such evaluation. These are done on a formal basis for a variety of purposes, as well as continuously on an informal basis in the process of performing our corporate finance functions such as raising capital, assisting in mergers and acquisitions, etc. The factors used in such evaluations and their importance and materiality to the investment community are areas in which I have developed expertise and had substantial experience over the last twenty-four years. Additionally, we have prepared a substantial number of analyses of market impact and damages in connection with numerous shareholder litigations.

4. Also included in Exhibit A is a list of the 23 cases in which I have testified at trial. Many of these matters have involved determinations of values of companies and/or securities based on actual situations and/or hypothetical assumptions, as well as the determination of materiality. More specifically, among the cases in which I have testified are the following:

A. In *U.S. Banknote Securities Litigation,* I testified as an expert witness on behalf of the plaintiff class (U.S.D.C., S. District of NY, J. Cedarbaum). The jury returned a verdict for plaintiffs and found substantial damages; defendants' expert had said there were none.

B. In *Geriatric and Medical Centers Securities Litigation,* I testified as an expert on behalf of the plaintiff class (U.S.D.C., E. District of Pa., J. Fullam). The jury returned a verdict for plaintiffs and found substantial damages; defendants' expert had said there were virtually none.

C. In *O & M Investment Partners v. Windon et al.,* I testified as an expert on behalf of the plaintiff (U.S.D.C., E. District of Pa., Judge Robert F. Kelly). The parties settled shortly thereafter; plaintiffs received a substantial payment.

D. In *Pennsylvania Enterprises Securities Litigation,* I testified as an expert on behalf of the plaintiff regarding issues of materiality. (U.S.D.C. for the E. District of Pa., J. Van Artsdalen). The judge found those items on which I opined to be material.

E. In *Kay Jewelers Securities Litigation,* I testified as an expert on behalf of the plaintiff class (U.S.D.C. for the E. District of Virginia, Alexandria Division). The parties settled shortly thereafter; plaintiffs received a substantial payment.

F. In *McKinley Allsopp, Inc. v. Jetborne International, Inc.,* I testified as an expert on behalf of the

defendant and counterclaimant (U.S.D.C. for the S. District of N.Y., J. Leval). The judge found for the defendant and counterclaimant and cited my testimony as a factor in establishing the proper standard of investment banking performance at issue.

G. In *I.A. Holdings Corporation Dissenter's Appraisal Action,* I testified as an expert on behalf of the dissenting stockholders (Court of Common Pleas, Del. Co., Pa., J. Lawhorne). The judge found for the dissenting stockholders awarding substantially the amount to which I testified.

H. In *GCA Corporation Securities Litigation,* I testified as an expert on behalf of the plaintiff class (U.S.D.C. for the District of Massachusetts, J. Caffrey). The parties settled shortly thereafter; plaintiffs received a substantial payment.

I. In *Baer v. Fidelco Growth Investors,* I testified for the defendants as to the fairness of the proposed exchange of cash, securities and real estate properties in a corporate reorganization. (Court of Common Pleas, Montgomery Co., Pa.). The judge found the exchange to be fair as I had testified.

J. In *Vadakin v. Vadakin,* I testified for the plaintiff as to the value of a privately held business (Ohio State Court, Marietta). The judge found for the plaintiff, awarding the value to which I testified, and requested my assistance in structuring an award.

Introduction and Summary

5. I have been retained by plaintiffs' counsel for the purpose of consulting on corporate governance and economic issues, and providing my expert evaluation and analysis of certain issues related to the terms of the settlement of this litigation, including certain therapeutic resolutions to be passed by Archer Daniels Midland's (ADM) Board of Directors as set forth in Exhibit B hereto. My

opinions are based on my professional experience including that of assisting in negotiating, structuring and evaluating numerous settlements of securities litigation matters.

6. I have reviewed documents, including the following:

- Consolidated and Amended Derivative Complaint, and Amendment and Supplement Thereto.
- Various proposed terms for settlement.
- National Association of Corporate Directors Blue Ribbon Commission on Director Professionalism—Report (summary).
- Council of Institutional Investors—Definitions of Independent Director and accompanying materials.
- Council of Institutional Investors Shareholder Bill of Rights.
- Numerous trade, business press and investment community articles and research and analyses of board structure and companion corporate governance, and effects on company performance and shareholder value.
- ADM daily share price and volume data for a period from before any kowledge of allegations was "in the market", to date.
- Daily and weekly market and industry index price levels for time periods as above.
- Insider trading data.
- ADM Proxy Statements.
- ADM Forms 10-K and Q.
- ADM annual and quarterly shareholder reports and/or press coverage thereof.
- News articles re: ADM.

- Brokerage firm securities analyst reports on ADM.
- Stipulation of Settlement, including Exhibit A thereto.
- Affidavit of John C. Coffee, Jr. (draft).

7. In my opinion, and based on my education, knowledge and experience, the value of the benefits to ADM from the settlement of the subject litigation is a *minimum* of $158 million, and is quite likely considerably larger.

Evaluation of Terms of Settlement

8. To my understanding, the benefits to ADM from the proposed resolution of the derivative litigation include the following:

A. Cash settlement of $8,000,000.

B. Adoption by the Board of Directors of the corporate governance measures and procedures described in Exhibit B hereto, the purpose of which (from an economic viewpoint) is to significantly reduce or eliminate the likelihood of recurrence of the types of action which led to the subject litigation.

C. Ending the very considerable expense, loss exposure and management distraction which would be caused if the litigation continued.

9. Although $8,000,000 in cash is straightforward, the *benefits* of its use are likely to well exceed this amount. That is, at least 51% of the $8,000,000 cash portion of the settlement is to be used to fund the activities of the independent audit committee and its counsel for a period of at least three years. To the extent this activity reduces the likelihood of recurrence of the type of action which led to the litigation, it increases the value of these reform measures substantially, which described below, is worth many multiples of the $8,000,000 cash amount.

10. The benefits of avoiding the costs referred to in paragraph 8B above can be addressed in two ways:

A. avoidance of such costs in the future, and qualification thereof, and

B. the amount, by observation of the effect on the market value of the Company, of the positive impact of such avoidance on the Company.

11. Attached as Exhibit C hereto is a copy of the "litigation" section of ADM's 1996 Form 10-K Report, which summarizes the outstanding litigation at the date thereof. As a reader can see, the list is long and substantial. I have seen no public discussion of estimated costs or exposure as a result of these matters. However, I believe at least $190 million has been publicly identified so far as amounts paid in fines and settlement payments; that amount does not include legal fees. It appears that $250 million may be a *very* conservative estimate of the direct costs of management's improper actions. To that must be added legal expenses, and the substantial distraction of management attention caused by defending and dealing with these matters. It appears that a *minimum* of $300 million would be the minimum cost of this item.

12. A. To derive an economic value from avoiding a recurrence of these actions and their costs, a percentage probability must be assigned to the likelihood of their recurrence, with and without the board reforms. This is a commonly accepted economic analysis technique known as expected value analysis, or as rational expectations analysis.[1]

[1] This technique is a basic economic tool often used to measure the value of events with multiple possible outcomes. To apply it, one must determine the cost of an event if it does occur, then assign a (percentage) factor to indicate its likelihood of occurrence. If (as in this case) there are two different likelihoods of occurrence given two different sets of assumptions (before and after implementation of the Corporate Governance Provisions), one can measure the difference between them as the cost of the event

Considering the numerous areas of business and number of product lines in which they occurred, the senior level of the management personnel involved (and their ties to those who dominated the board) and the degree of planning and execution necessary to implement the actions, it is difficult to believe the actions would not likely continue absent the Board of Directors reforms. With the reforms in place *and funded* to ensure the independence of overseers, recurrence seems highly unlikely and difficult to achieve. A fair estimate of the difference between likelihood of recurrence and not, is 50% in my opinion; that is 70 to 80% chance of recurrence without reforms versus 20 to 30% with reforms. An observer can make his own judgment as to percentage likelihood, but 20 to 30% seems very conservative (high). To quantify the economic value, then, using the expected value methodology, multiply the cost of recurrence ($300 million minimum) times the differential in likelihood due to reforms (50%) for a result of $150 million *minimum*.

B. In determining the proper percentage likelihood of recurrence of the wrongdoing, I note the following from Professor Coffee's Affidavit:

> In general, I believe the Corporate Governance Provisions represent more or less the "state of the art" in American corporate governance today. . . . In addition, beyond these corporate governance provisions, there are special legal compliance provisions

it if does occur, multiplied times the difference between the likelihood factors. This expected value analysis technique is taught in basic economic courses. It is used constantly by participants in the financial markets, both explicitly and implicitly, as a regular part of quantifying the likely effect on companies or entities of various possible future events, and as a means of reducing risks of various events occurring to dollar values. I have used this technique as the basis for determining alternative values as a basis for damages in numerous litigation matters, including in testimony which became the basis for awards by fact finders.

> that I believe are of special value to a corporation with Archer Daniels Midland's ("ADM") history.
>
> More importantly, the definition of "outside director" in the Corporate Governance Provisions is tighter and more restrictive than those set forth in most of the well-known contemporary corporate governance guidelines.

In addition, he supports the creation of the "lead director" role and its value to the enterprise. Further:

> Collectively, the combination of the lead director provision, the annual board review, and the requirements that (a) the Audit Committee be composed "solely of outside directors" for the next three years . . . represent in my judgment significant steps to facilitate board independence and to end the apparent managerial domination of the ADM board. Although it is never possible to predict that these changes will of necessity be successful, there is frankly little more that can be done from a corporate governance perspective in terms of board structure or procedures.

C. Adding to the benefits of the preventive actions and enhancing their value is the speed with which the improvements in corporate governance are being implemented. The provisions of Exhibit A to the Stipulation of Settlement are to be implemented within 60 days. A review of literature suggests this is considerably faster and further reaching than many corporate governance improvements. See Exhibit E.

13. A. I have reviewed the stock price and volume data for Archer Daniels Midland ("ADM") since July of 1994 as well as news releases and articles during that time to determine the likely impact on overall market capitalization of implementing the Board of Directors reforms in the settlement at issue. The likely market effect of this action is not entirely clear from the analysis as a) financial results or other information was often reported

on or about the same dates as such news as the announcements of the recommendations of the corporate governance committee and may have overshadowed them and b) even though some recommendations for improvement were made (for example in early 1996), the full board initially did not adopt them and in fact appeared to resist them. However, despite these factors, I believe a significant market value impact can be observed. Based on this empirical data, the magnitude of the proposed change could well impact the share price in a range from 0 to as much as $2.00 per share. An effect of .50 to 1.00 is highly likely, with a midpoint of $0.75. Based on the 533,418,000 shares outstanding at May 30, 1997, the effect on total market capitalization would be as follows::

Amount Per Share	*Total Market Capitalization Effect*
$0.25	$ 133,354,500
0.50	266,709,000
0.75	400,063,500
1.00	533,418,000
1.50	800,127,000
2.00	1,066,836,000

To place these figures in context, on May 30, 1997 the stock price was $20.00; the total market capitalization was $10,668,360,000. Using a $0.75 figure from the table above, the aggregate market impact of $400,063,500 =3.75% of $10,668,360,000. In surveys of management quality as perceived by market participants and competitors, ADM has ranked among the worst perceived. The investment community places significant value on management, rewarding companies with high quality management with premium evaluations and applying discounts to those perceived as poor. A 3.75% change in market value is certainly within these parameters.

B. i. I performed a search of academic literature, and trade and business press and investment community publi-

cations, to attempt to determine if there was published information bearing on the value of improving corporate governance and/or providing a framework with which to compare the ADM settlement provisions.

ii. Enclosed as Exhibit D is a copy of an article which appeared in *The Journal of Finance*, Vol. LI, No. 1, March 1996, entitled "Shareholder Activism by Institutional Investors: Evidence from CalPERS" by Michael P. Smith. I believe the article is instructive in that it measures shareholder wealth effects of improved corporate governance structures and procedures, and concludes that "Shareholder wealth increases for firms that adopt [improved corporate governance] or settle and decreases for firms that resist" (from the Abstract). The article concludes "Overall, the evidence indicates that shareholder activism is largely successful in changing governance structure and, when successful, results in a statistically significant increase in shareholder wealth."

iii. Enclosed as Exhibit E are copies of four articles which describe in considerable detail the benefits of improved corporate governance and the actions of various organizations of investors, and of academics to study and promote such improvements, as well as significant information allowing a comparison of the ADM settlement provisions with actual practices at leading companies and generally acknowledged "best practices". The articles cite the following notable studies and reports:

- The General Motors study and report, which has become a blueprint for numerous other companies' policies.
- The Calpers study and review process which graded boards on various measures of effective, independent governance structures and proocesses.
- A study of the Investor Responsibility Research Centre of guidelines developed by boards at S&P 500 companies.

- A book by Ralph Ward, editor of the *Corporate Board* journal, entitled *The 21st Century Corporate Board*, which describes, *inter alia*, how the General Motors guidelines fall short in several areas:

  > Despite some solid reforms, many of the governance tools to be used were carefully left blank. Items such as the committee structure, board size, mix of inside and outside directors, and former chief executive board membership waffled with "as the board may consider appropriate" qualifiers.

  Clearly the ADM settlement provisions are significantly better than these guidelines.
- The National Council of Individual Investors survey ranking companies by their level of "shareholder accountability".
- A study by two Canadian academics in connection with a 1997 scheduled review of the Canada Business Corporations Act.
- A study by *Chief Executive* of best and worst boards including extensive discussion of criteria and results.

A review of these articles confirms that the ADM provisions to be enacted will move it from among the worst (as specifically cited many times), to the head of the best current practices group. Items which are "suggested" or "as deemed appropriate" by other guidelines are *required* in the ADM provisions. Structures are set in writing, and the independent audit committee—charged with monitoring, oversight and training and funded independently—appears unique based on this review.

These observations strongly support my opinions as to the relative percentage likelihood of recurrence of the vio-

lations, and the value of the ADM therapeutic settlement provisions.

14. I have not attempted to place a specific dollar figure on management's time and attention devoted to the defense and administration of this matter but note that in Section III of the Stipulation of Settlement, Defendants state:

> Despite their assertions, the Director Defendants have concluded that the further conduct of the Litigation would be protracted and expensive, and that it is desirable that the Litigation be fully and finally settled in the manner and upon the terms and conditions set forth in this Stipulation in order to limit further expense, inconvenience and distraction, to dispose of burdensome and protracted litigation, and to permit the operation of ADM's business without further expensive litigation and the distraction and diversion of ADM's executive personnel with respect to matters in issue in the Litigation.
>
> Moreover, the Director Defendants recognize that the procedures and measures that are set forth in Exhibit A, and which the Company will implement as part of the Settlement, will provide substantial benefits and protections to the Company and its shareholders.

15. I declare under penalty of perjury, pursuant to 28 U.S.C. Section 1746, that the foregoing statements are true and correct.

/s/ R. Alan Miller
R. ALAN MILLER
President
Philadelphia Investment
Banking Company

Date 6/26/97

[Exhibits Omitted in Printing]

[Filed Jul. 2, 1997]

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS

[Caption Omitted in Printing]

MEMORANDUM OF LAW
IN SUPPORT OF SETTLEMENT

NOW COMES the Nominal Defendant, ARCHER DANIELS MIDLAND COMPANY, a Delaware corporation, by KEHART, SHAFTER & WEBBER, P.C. and WILLIAMS & CONNOLLY, its attorneys, and in support of the settlement proposed herein, respectfully submits the following Memorandum of Law.

STATEMENT OF FACTS

A. BACKGROUND.

The present litigation arose[1] immediately following the public disclosure that the United States Department of Justice was investigating alleged violations of federal antitrust laws[2] by Archer Daniels Midland Company, a Delaware corporation ("ADM"). Generally, the Plaintiffs alleged (within their original as well as subsequent

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[1] The litigation was filed initially in the United States District Court for the Northern District of Illinois as Cause No. 95-4006, and was transferred to the United States District Court for the Central District of Illinois by the Honorable Ruben Castillo, United States District Judge, by order dated October 31, 1995.

[2] The investigation by the United States Department of Justice included markets for three products—lysine, citric acid, and high fructose corn syrup.

pleading(s)) that the Defendants [3] breached fiduciary duties owed to ADM (*see* d/e 28, ¶ 26), but the Plaintiffs concede that

> [e]ach of the Director Defendants has denied and continues to deny each and all of the claims and contentions alleged by the Plaintiffs. . . .

(d/e 60, Ex. A, p. 5).

This litigation purportedly was brought by the Plaintiffs, in a derivative capacity as shareholders, for the benefit of ADM. (*See* d/e 28, ¶ 13). Similar litigation was also advanced in the Court of Chancery for the State of Delaware, entitled *In Re Archer Daniels Midland Company Derivative Litigation*, Consolidated No. 14403. The settlement proposal presently before the United States District Court for the Central District of Illinois (the "District Court") would resolve all shareholder derivative litigation involving ADM and based upon action or inaction which formed (or could have formed) the basis of the present litigation.

B. PROCEDURAL HISTORY.

The present litigation opened in the District Court on September 22, 1995 (d/e 1).[4] On December 27, 1995, the Defendants and ADM moved to dismiss the Plaintiffs' pleading (d/e 2), a motion which was granted on April 26, 1996. The Plaintiffs filed an amended pleading on May 17, 1996 (d/e 28), which pleading also was met with a motion to dismiss, filed June 7, 1996 (d/e 29).

[3] The Defendants are: Dwayne O. Andreas, Ralph Bruce, John H. Daniels, Howard G. Buffett, Lowell W. Andreas, James R. Randall, Michael D. Andreas, H. D. Hale, O. Glenn Webb, Martin Andreas, Margaretta Rockefeller, F. Ross Johnson, Ray A. Goldberg, John K. Vanier, Shreve H. Archer, Jr., M. Brian Mulroney, and Robert S. Strauss.

[4] *Cf.* fn. 1.

Although the Plaintiffs sought leave to supplement their pleading (*see* d/e 43, 49), the pleading on file remains subject to a motion to dismiss by the Defendants and ADM.

On May 30, 1997, the parties submitted an agreed motion requesting preliminary approval of a proposed settlement in order to provide notice to shareholders of ADM (*see* d/e 60). The District Court, by the Honorable Harold A. Baker, then granted the agreed motion and scheduled the matter for hearing on July 7, 1997 to determine whether the proposed settlement is fair, reasonable, and adequate (*see* d/e 62).

C. SETTLEMENT.

1. Introduction.

Following extensive communications, discussions, meetings, and negotiations, the parties entered into a Memorandum of Understanding, dated May 29, 1997, the terms of which constitute the nucleus of the Stipulation of Settlement (the "Stipulation") filed with the District Court on May 30, 1997 (d/e 60).

The proposed settlement provides that the Defendants [5] would be "fully, finally and forever released, relinquished and discharged [from] all Settled Claims." [6] (d/e 60,

[5] The release does not apply to all of the Defendants, and ADM would retain claims, if any, against one Defendant, a former director.

[6] "Settled Claims" is defined as in the Stipulation and the Memorandum of Understanding as any and all causes of action, suits, demands, claims, matters and issues, whether known or unknown, which have been, could have been, or in the future might be asserted, advanced or alleged in any of the Actions (as defined herein) or in any court or arbitration proceeding (including, without limitation, any claims, actions or demands arising under any federal or state law relating to alleged fraud, breach of any duty, negligence, recklessness, violations of federal or state securities laws,

p. 18). In exchange for this release of claims, Eight Million Dollars ($8,000,000.00) would be provided to ADM less fees and expenses approved by the District Court, and ADM would implement certain corporate governance changes.

2. Settlement Funds.

On May 30, 1997, ADM received Eight Million Dollars ($8,000,000.00), paid to ADM by the Defendants or on their behalf. These funds are subject to conditions and restrictions, as described within the Stipulation, but are invested and presently earning interest which also will be paid to ADM upon final approval.[7] These settlement funds are (and will be) invested in securities either issued or collateralized by the United States.

From this $8 Million (plus interest), the attorneys representing the Plaintiffs, and counsel representing shareholders in other derivative litigation, will request compensation, subject to approval by the District Court.

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violations of federal or state antitrust laws or otherwise) by or on behalf of the Company (as defined herein), by any shareholder of said Company derivatively on its behalf, or by any named plaintiff in the Actions (as defined herein) on their own behalf or on behalf of any record or beneficial holder of the stock of the Company (as defined herein), whether individual, class, derivative, representative, legal, equitable, or any other type in any other capacity, which claims have arisen, could have arisen, arise now or hereafter arise out of, or relate in any manner to the allegations, transactions, matters or occurrences, representations, acts or omissions, or any series thereof, involved, set forth, referred to, or related to any of the pleadings in the Actions (as defined herein) against the Company (as defined herein) and/or any of the Individual Defendants (as defined herein), provided, however, that Settled Claims shall not include any claims which the Company may have against Andreas (as defined herein), Wilson (as defined herein), or the Excluded Persons (as defined herein), which claims shall be reserved to the Company in its sole discretion.

[7] As of July 7, 1997, the settlement proceeds should equal $8,039,600.00.

The remaining funds[8] will be utilized in support of the Audit Committee of the Board of Directors of ADM in the performance of its duties to ensure training or educational efforts and implementation of corporate governance changes.

3. Corporate Governance.

If approved, the settlement includes changes in corporate governance as discussed within the agreed motion filed herein on May 30, 1997 (d/e 60).

First, if the Chairman of the Board is not an "outside director" (the definition of which is discussed later herein), then the outside directors will elect an outside director to act as Vice-Chairman to preside over meetings of non-management directors and of the Governance Committee. Second, the Audit Committee, comprised *solely* of outside directors, will be charged with the task of overseeing issues of legal compliance with state or federal laws relating to antitrust, discrimination, environmental, securities and disclosure, and foreign corrupt practices act enforcement. The Audit Committee also will be charged to ensure that reporting systems provide the Board with adequate and accurate information. The Audit Committee will receive regular reports from senior management and likewise will report regularly to the Board as a whole. Outside independent legal counsel will be retained (and selected) by the Audit Committee.

Third, the Governance Committee will establish and approve performance criteria for evaluation of the Chief Executive Officer, assess effectiveness of the Board (and committees), and the Governance Committee's performance criteria and evaluation process will be disclosed in proxy statements for the annual meeting of shareholders.

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[8] Certain of the funds may be utilized to pay costs and expenses necessarily incurred in providing notices or information to shareholders by ADM.

Fourth, total compensation to be paid to non-employee directors (for a period of three (3) years) will not exceed $100,000 per annum, and one-half of this compensation will be paid in ADM stock. Fifth, to the extent permissible, voting by shareholders will be confidential.

Sixth, the Compensation Committee and Nominating Committee, as well as the Audit Committee, will be comprised exclusively of outside directors.

Seventh, a majority of the Board will be comprised of outside directors, and the number of direct management representation on the Board is limited to two individuals plus the Chief Executive Officer. Furthermore, the term "outside director"[9] was defined to mean a director who (a) is neither a current employee nor former member of senior management of ADM or an affiliate; (b) does not have a business or professional relationship which is material to ADM or the director; (c) does not have a close familial relationship with any member of senior management of ADM; (d) is not an officer of a company of which ADM's Chairman or CEO is also a board member; (e) is not personally receiving compensation from ADM in any capacity other than as a director; and (f) does not personally receive, nor is he an employee of a foundation, university or foundation which receives, grants or endowments from ADM which are material to ADM or the recipient.

D. OBJECTIONS.

As of June 30, 1996, the number of shareholders of ADM's common stock, as recorded on the books of ADM, was 35,431. In accordance with the District Court's order

[9] On June 17, 1997, the *Wall Street Journal* reported that the California Public Employees' Retirement System (Calpers), a leading advocate of corporate governance standards (and stringent definitions of "independence"), was unable to establish for itself a set of corporate governance standards.

of May 30, 1997, ADM sent approximately 243,000 notices,[10] for delivery to persons with interests in ADM's stock. These notices advised the recipient (i) of the litigation, (ii) of the proposed settlement of the litigation, (iii) of the terms of the proposed settlement, and (iv) of the right, and manner in which, to present any objection. As of June 30, 1997,[11] ADM is aware of the existence of objections presented by seven (7) shareholders, either individually or jointly.

In alphabetical order of the objectors, objections were received from the following:

(a) Berns, Mitchell—objecting to potential attorneys' fee award;

(b) Chiara, John P.—objecting to potential attorneys' fee award;

(c) Gilbert, John J. and Glotzer, Martin—objecting because governance matters do not require cumulative voting;

(d) Pauly, Charles W. and Elizabeth D.—objecting because settlement award and benefit is too little or too great; and

(e) Scott, Peter D.—objecting to potential attorneys' fee award.

ADM takes no position as to the objections of Messrs. Berns, Chiara and Scott. However, the objections of Messrs. Gilbert and Glotzer and the objections of Mr. and Mrs. Pauly are discussed by ADM herein.

[10] The number of notices greatly exceed the number of shareholders designated on the books of ADM because numerous shareholders hold shares for the benefit of others, often in street names, or in the name of a broker or financial advisor.

[11] Because this memorandum is submitted prior to the date by which objections may be submitted, ADM will seek to supplement this memorandum to dismiss later filed objections, if any.

ARGUMENT

A. THE STANDARDS APPLICABLE TO THE DISTRICT COURT'S REVIEW.

The present litigation is a shareholders derivative action, purportedly brought on behalf of ADM, pursuant to *Fed. R. Civ. P.* 23.1. The motion presently before the District Court is brought because of the directive of *Fed. R. Civ. P.* 23.1 that

> [t]he action shall not be dismissed or compromised without the approval of the court, and notice of the proposed dismissal or compromise shall be given to shareholders or members in such manner as the court directs.

While the proponents of the settlement must demonstrate that the settlement is fair, adequate and reasonable (*United Founders Life Insurance Co. v. Consumers National Life Insurance Co.*, 447 F.2d 647 (7th Cir. 1971); *Susquehanna Corp. v. Korholz*, 84 F.R.D. 316 (N.D. Ill. 1979)), settlement of shareholders derivative actions are favored and a presumption in favor of approving settlements exists. *Donovan v. Robbins*, 752 F.2d 1170 (7th Cir. 1985). Whether the proposed settlement is fair rests in the sound discretion of the District Court. *See Susquehanna Corp., supra.* The District Court should not, however, decide the merits of the action and should not substitute its judgment for the business judgment of the parties who reached the accord. *See Id.*

In its evaluation of the proposed settlement, the District must

> weigh the probabilities and possibilities of victory or defeat as indicated by the legal or factual situation presented and determine whether the compromise, taken as a whole, is in the best interests of the corporation and its shareholders.

United Founders Life Insurance Co., 447 F.2d at 655, *quoting Winkelman v. General Motors Corp.*, 48 F.Supp. 490, 493 (S.D.N.Y. 1942). The District Court also should consider the following factors: (i) the strength of the plaintiffs' case on the merits; (ii) the complexity, length and expense of continued litigation; (iii) the degree of opposition to the settlement; (iv) the presence of collusion in gaining a settlement; (v) the opinion of competent counsel as to the reasonableness of the settlement; and (vi) the stage of the proceedings and the amount of discovery completed. *Donovan v. Fitzsimmons*, 778 F.2d 298 (7th Cir. 1985); *Susquehanna Corp. v. Korholz*, 84 F.R.D. 316 (N.D. Ill. 1979). As the *Susquehanna Corp.* court observed,

> [w]hen, in a derivative action, a settlement proposal is arrived at after arms-length negotiations have been conducted, it is clear that sufficient discovery has been taken to allow the court and the parties to act intelligently, the counsel involved are competent and experienced, and the numbers of objectors, or the interest they represent, is not large, it may properly be presumed that the agreement is fair and adequate.

84 F.R.D. at 321.

The District Court is not to use the settlement hearing as a trial or a rehearsal of a trial on the merits of the litigation. *Levin v. Mississippi River Corp.*, 59 F.R.D. 353 (S.D.N.Y. 1973), *citing Newman v. Stein*, 464 F.2d 689 (2nd Cir.), *cert. denied* 409 U.S. 1039 (1972); *Glicken v. Bradford*, 35 F.R.D. 144 (S.D.N.Y. 1964). Indeed, an evidentiary hearing, while certainly permitted, is not required. Rather, it is sufficient for the District Court to accept memoranda in support of the settlement and to assure itself that there is an adequate record for evaluating the settlement. *Patterson v. Stovall*, 528 F.2d 108 (7th Cir. 1976).

The present litigation is controlled by the law of the State of Delaware, because ADM is incorporated in Dela-

ware, and the law of the state of incorporation is controlling with respect to the fiduciary duties owed by directors to the corporation. *See Treco, Inc. v. Land of Lincoln Savings & Loan,* 749 F.2d 374 (7th Cir. 1984). In Delaware, the business and affairs of a corporation are managed by or under the direction of the Board of Directors, and such directors are charged with fiduciary obligations, including the duty of loyalty and the duty of care. *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345 (Del. 1993); 8 Del. C. § 141(a). While directors are charged with fiduciary obligations, such directors fulfill those duties when they exercise business judgment, in good faith, in making decisions concerning the corporate entity. When a director acts in good faith, the director enjoys a presumption of sound business judgment that a court will not disturb so long as a rational business purpose may be attributed to the director's decision.

> In the absence of fraud, bad faith, gross overreaching or abuse of discretion, courts will not interfere with the exercise of business judgment by corporate directors.

Panter v. Marshall Field & Co., 646 F.2d 271, 293 (7th Cir. 1981) (applying Delaware law); *Cf. Cede & Co.*, 634 A.2d 345, *supra*. In the present litigation, the Defendants are also shielded by Article XIV of the ADM Certificate of Incorporation, permitted by Delaware law, and which includes a provision:

> A director of the Corporation shall have no personal liability to the corporation or its stockholders for monetary damages for breach of his fiduciary duty as a director, provided however this Article shall not eliminate or limit the liability of a director (1) for any breach of director's duty of loyalty to the Corporation or its stockholders; (2) for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law; (3) for the unlawful payment of dividends or unlawful stock repurchases under § 174 of the General Corporation Law of the State of Delaware; or (4) for any transaction from which the director derived an improper personal benefit. This Article shall not eliminate or limit the liability of a director for any act or omission occurring prior to the effective date of this Article.

Thus, the Certificate of Incorporation of ADM provides a further hurdle for the Plaintiffs to overcome in any successful litigation against the Defendants for breach of fiduciary obligations.

B. THE PRESENT LITIGATION IS SUBJECT TO INVOLUNTARY DISMISSAL UNDER DELAWARE LAW.

Shareholder derivative litigation brings to the court a cause of action which properly belongs to the corporation (*Rales v. Blasband,* 634 A.2d 927 (Del. 1993)), and because the litigation is brought purportedly on behalf of the corporation, any damages recovered are paid to the corporation. *See Sternberg v. O'Neil,* 550 A.2d 1105 (Del. 1988); *Zapata Corporation v. Maldonado,* 430 A.2d 779 (Del. 1981). Furthermore, the directors, not the shareholders, manage the business and affairs of the corporation. *Aronson v. Lewis,* 473 A.2d 805 (Del. 1984).

Arising from the principle, that derivative litigation belongs to the corporation, is the requirement that the shareholders make demand upon the Board prior to filing shareholder litigation. *See Spiegel v. Buntrock,* 571 A.2d 767 (Del. 1990). This requirement of a pre-suit demand is designed

> to assure that the stockholder affords the corporation the opportunity to address an alleged wrong without litigation, to decide whether to invest the resources of the corporation in litigation, and to control any litigation which does occur.

Id, 571 A.2d at 773. In *Aronson v. Lewis*, 473 A.2d, 805 (Del. 1984), the Supreme Court of Delaware stated

> By its very nature the derivative action impinges on the managerial freedom of directors. Hence, the demand requirement. . . exists at the threshold, first to insure that a stockholder exhausts is [*sic*] intracorporate remedies, and then to provide a safeguard against strike suits. Thus, by promoting this form of alternate dispute resolution, rather than immediate recourse to litigation, the demand requirement is a recognition of the fundamental precept that directors manage the business and affairs of corporations.

473 A.2d at 811-12 (footnote omitted).

The requirement of making a pre-suit demand is strictly enforced by the courts. Where a putative derivative plaintiff seeks to institute an action on a corporation's behalf without demand on the Board, the plaintiff must allege, *with particularity*, specific *facts* demonstrating why such demand should be excused. *See Fed. R. Civ.* 23.1; Del. Ch. Rule 23.1; *Stepak v. Dean*, 434 A.2d 388, 390 (Del. Ch. 1981). The failure to make a demand or to plead legally sufficient facts demonstrating that demand should be excused mandates dismissal of the complaint. *Pogostin v. Rice*, 480 A.2d 619 (Del. 1984); *Aronson v. Lewis*, 473 A.2d 805 (Del. 1984).

In the present litigation, the Plaintiffs did not make a pre-suit demand, and it is the position of ADM that the Plaintiffs failed to meet their heavy burden in pleading specific facts which would demonstrate that a majority of the Board was either (1) so self-interested in the challenged conduct or (2) so dominated and controlled by the alleged corporate wrongdoer(s) to reverse the customary presumption of independence. *See Levine v. Smith*, 591 A.2d 194 (Del. 1991); *Pogostin v. Rice*, 480 A.2d 619 (Del. 1984).

As is set forth within ADM's motion to dismiss the complaint (d/e 29) and as is explained within ADM's

memorandum in support of that motion (d/e 31), the Plaintiffs face a substantial burden in attempting to overcome ADM's motion to dismiss the litigation in its entirety for failure to make the requisite demand upon the Board of Directors, and the Plaintiffs' failure to plead particularized facts sufficient to excuse this demand. Furthermore, the Certificate of Incorporation of ADM includes a substantial shield for the Defendants from liability for monetary damages allegedly arising from breaches of the duty of care. Thus, the present litigation is similar to shareholder derivative actions in general as being "notoriously difficult and unpredictable." *Schimmel v. Goldman*, 57 F.R.D. 481, 487 (S.D.N.Y. 1973); *Cf. Zimmerman v. Bell*, 800 F.2d 386 (4th Cir. 1986); *Maher v. Zapata Corp.* 714 F.2d 436 (5th Cir. 1983); *Republic National Life Insurance Co. v. Beasley*, 73 F.R.D. 658 (S.D.N.Y. 1977).

C. THE PROPOSED SETTLEMENT IS IN THE BEST INTEREST OF ADM AND ITS SHAREHOLDERS.

The proposed settlement presently before the District Court for approval involves various elements. That portion of the proposed settlement which involves payment of $8 Million by the Defendants, or on their behalf, and that aspect which provides that certain claims are reserved to ADM, are straightforward. Those elements of the proposed settlement involving issues of corporate governance are, in reality, the linchpin of the proposed settlement. Such "corporate therapeutics" for the benefit of the corporation may, by themselves, support a derivative settlement. *Bell Atlantic Corp. v. Bolger*, 2 F.3d 1034 (3rd Cir. 1993); *Granada Investment, Inc. v. DWG Corp.*, 962 F.2d 1203 (6th Cir. 1992); *Zimmerman v. Bell*, 800 F.2d 386 (4th Cir. 1986); *Maher v. Zapata Corp.* 714 F.2d 436 (5th Cir. 1983); *Levin v. Mississippi River Corp.*, 59 F.R.D. 353 (S.D.N.Y.), *affirmed* 486 F.2d 1398 (2nd Cir.), *cert. denied*, 414 U.S. 1112

(1973); and *Cf. Mills v. Electric Auto-Lite Co.*, 396 U.S. 375 (1970) (non-monetary recovery on merits does not preclude award of fees). The corporate therapeutics involved in the presently proposed settlement are set forth clearly within the Stipulation of Settlement (d/e 60), and need not be repeated here. Suffice to say that these corporate therapeutics include substantial changes in the manner in which issues are presented and resolved by the ADM Board. ADM presents in support of its position on this issue the Affidavit of Professor Michael P. Dooley, the William S. Potter Professor of Law at the University of Virginia.

In *Bell Atlantic Corp.*, the court assessed whether a settlement which mandated structural changes in the corporate governance of the corporation was a fair settlement of a shareholder derivative action. The court noted the difficulty in measuring the value in the non-monetary benefit, and an objector to the settlement charged that these corporate governance changes were duplicative of changes already made and that the change upon which the settlement was premised amounted to little more than a promise to obey the law. The United States Court of Appeals for the Third Circuit rejected these objections and held that the changes in corporate governance brought about by the settlement were broader and more inclusive than changes to which the company had agreed in an action with the State Attorney General, and the court noted that the agreement not only ensured that the corporation would follow the law, but provided specific mechanisms to ensure employees of the corporation and its subsidiaries behaved appropriately. *See Bell Atlantic Corporation*, 2 F.3d at 1312. The *Bell Atlantic Corp.* court also noted the improbability of the plaintiff's success on the merits and the fact that fewer than thirty (30) of the corporate entity's 1.1 million shareholders objected to the proposed settlement.

In *Zimmerman*, a shareholder derivative action arising out of the alleged mishandling of a takeover attempt, the

court considered a settlement which required the corporation to adopt a detailed statement of procedures to be followed in the event of a future tender offer or takeover bid. Two out of "tens of thousands" of shareholders objected to the proposed settlement. The *Zimmerman* court noted

> Influencing the future conduct of management may serve the interests of the corporation as fully as a recovery for past misconduct, and a settlement may be accepted "even though no direct monetary benefits are paid by the defendants to the corporation." Here, the Statement of Policy provides guidelines for future management responses to tender offers and takeover bids, the very situation that prompted these various complaints.

800 F.2d at 390, *quoting Maher v. Zapata Corp.*, 714 F.2d 436, 466 (5th Cir. 1983). The *Zimmerman* court noted that the majority of directors were outside directors, that the Board obtained outside advice from an investment banker, and that settlement of shareholder derivative actions are favored because of the complexity of the litigation, and the Court of Appeals held that the district court did not abuse its discretion in approving the settlement.

In *Granada Investments*, a minority shareholder brought a derivative action against a corporation and its directors, which included controlling shareholders. The *Granada Investments* plaintiff alleged breaches of fiduciary duties and securities law violations stemming from claims of self-dealing on the part of controlling shareholders. The district court approved a settlement which called for the court to designate three new directors with no familial relationship to any party. The settlement called for these new directors to serve on the audit and compensation committees and created a special committee to review and approve incentive and bonus compensation, inter-

corporate transactions more than $500,000, as well as other transactions which could potentially involve self-dealing. The United States court [*sic*] of Appeals for the Sixth Circuit, in *Granada Investment*, noted:

> Admittedly, the fairness of a settlement is more difficult to determine when non-pecuniary benefits are provided to the corporation. Nonetheless, [the corporation] was released from all liability based on claims that might have been asserted by [the plaintiff]. In addition, the settlement called for changes in corporate governance. Against the background of a Posner-dominated board, the settlement provided for three new strategically placed directors and for a new special committee with oversight powers.

962 F.2d at 1206; *Cf. Levin*, 59 F.R.D. at 367, fn. 38 ("the fact that the form of the settlement decided upon is somewhat unusual in that it includes some benefits which cannot be evaluated in financial terms, does not militate against its acceptance; the parties are permitted great freedom in shaping the form of settlement consideration").

Finally, in *In Re Caremark International, Inc. Derivative Litigation*, 1996 WL 549894 (Del. Ch.), the court approved settlement of derivative claims following indictment and a guilty plea by the corporate entity to federal charges stemming from its unlawful payment of medical referral fees. Prior to the settlement with the derivative plaintiffs, the corporation's board had taken several steps aimed at increasing management supervision, modifying company policies concerning referral fees and strengthening its internal audit plan. In settling the derivative claims, the company and its directors agreed to additional governance changes, but the director defendants paid no money to the company. The *Caremark* court stated

> In light of the fact that the *Caremark* board already has a functioning committee overseeing corporate compliance, the changes in corporate practice that

> are presented as consideration for the settlement do not impress one as very significant. Nevertheless, that consideration appears fully adequate to support dismissal of the derivative claims of director fault asserted, because those claims find no substantial evidentiary support in the record and quite likely were susceptible to a motion to dismiss in all events.

1996 WL 549894 at page 12.

In the present case, the corporate therapeutic benefits which are received are of a type which could not have been attained by the Plaintiffs had they been successful in the litigation. Furthermore, the monies paid by the Defendants, or on their behalf, constitute funds which most probably would not be recovered by the Plaintiffs should the litigation continue. Thus, the monetary benefits received, taken together with the corporate therapeutic benefits, constitute more than substantial consideration for the proposed settlement to be deemed fair, adequate, and reasonable.

D. THE OBJECTIONS TO SETTLEMENT SHOULD BE OVERRULED.

As set forth previously, the objections of Messrs. Berns, Chiara and Scott are directed toward the request for attorney's fees which may be presented herein by the Plaintiffs. ADM takes no position as to these objections. The objections of Mr. and Mrs. Pauly, and the objections of John Gilbert and Martin Glotzer, are directed more to the substance of the settlement, and ADM responds thereto.

Mr. and Mrs. Pauly object because they assert that if the litigation brought by the Plaintiffs had merit, the settlement is insufficient in comparison to the monies which ADM might receive at the conclusion of the litigation, and that if the litigation is without merit, the Plaintiffs should receive nothing. Simply because the monetary amount proposed in a settlement is a fraction of what

could possibly be recovered does not render the proposed settlement inadequate or unfair. *Susquehanna Corp. v. Korholz*, 84 F.R.D. 316, 322 (N.D. Ill. 1979); *City of Detroit v. Grinnell Corp.*, 495 F.2d 448 (2nd Cir. 1974). Indeed, a proposed settlement is a compromise. Even if the cause of action asserted by the Plaintiffs was meritorious and would be successful, there is no guarantee that the monies recovered would be equal to or exceed the funds received in settlement or would exceed the value of the corporate therapeutics involved in the presently proposed settlement. Thus, the objections or Mr. and Mrs. Pauly are no different from potential objections to the settlement of any litigation where liability is contested, and the District Court should overrule those objections.

Mr. Gilbert and Mr. Glotzer present an objection, asserting that the corporate therapeutics, while perhaps beneficial, "do not go far enough". In essence, Mr. Gilbert and Mr. Glotzer ask the District Court to impose an additional term into the settlement, requiring cumulative voting. Mr. Gilbert and Mr. Glotzer state that approximately twenty-five percent (25%) of the shareholders voting in the most recent election voted for a proposal which would require cumulative voting, but they fail to acknowledge fully that the vast majority of shareholders voting on the issue voted against such a proposal. Furthermore, the term which these individuals propose to include in the settlement has not been the subject of negotiation, nor has it been the subject of the notice sent to the shareholders. Quite simply, this term might cause the number of objectors to increase, something which the District Court cannot divine. It is not up to the District Court to reopen and enter into negotiations in the hope of improving or changing the settlement in order to meet objections. *Levin v. Mississippi River Corp.*, 59 F.R.D. 353, 361 (S.D.N.Y. 1973). The settlement which is presently before the District Court is a matter which was the subject of intense negotiations and compromise. The additional term which is requested by Messrs. Gilbert and

Glotzer was not the subject of those negotiations, and is not properly brought within the settlement proposed.

For these reasons, the District Court should overrule the objections to the proposed settlement and approve the settlement in the form presented by the parties.

CONCLUSION

The settlement presently before the District Court is beneficial to ADM and its shareholders. Furthermore, the settlement terminates the risk, uncertainty, and distraction which accrues from all shareholder derivative litigation. Finally, the settlement provides benefit to the shareholders of ADM which benefit might not otherwise be available from litigation, and the corporate therapeutics which are included within the settlement most certainly would not be available solely as a result of continued litigation, even if successful.

The objections, filed to date which are directed to the substance of the settlement, as opposed to the potential claim for attorney's fees, lack merit in their entirety. One objection would effectively bar settlement in any litigation requiring court approval where liability is contested. The other objection involves a request by certain shareholders to require cumulative voting, which request was opposed by a majority of the shareholders of ADM during the last election where this issue was raised. If cumulative voting is to be instituted at ADM, such is more properly the result of democratic voting as opposed to judicial fiat.

For the reasons stated herein, the settlement proposed by the parties should be approved in its entirety.

[Listing of Counsel Omitted]

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

[Caption Omitted in Printing]

AFFIDAVIT OF MICHAEL P. DOOLEY

Michael P. Dooley, being duly sworn, deposes and says:

1. I am the William S. Potter Professor of Law at the University of Virginia. I have taught Corporation Law and related subjects since 1968 with a special emphasis on corporate governance. Among the courses I have taught are Corporate Governance and Finance and Courts and Corporate Governance, the latter in the Law School's LL.M. Judge's Program. I am the Reporter for the American Bar Association's Model Business Corporation Act and a member of the ABA's Committee on Corporate Laws and Corporate Practice Committee. I have also served as a member of the ABA's liaison committee for the American Law Institute's Corporate Governance Project and as a member of the Legal Advisory Committee to the New York Stock Exchange. I have been a consultant to or expert witness for a number of publicly held corporations on a variety of corporate governance matters and have served in similar capacities for the Attorney General of the Commonwealth of Virginia and the Virginia General Assembly. My recent publications in this area include "Two Models of Corporate Governance," 47 *Bus. Law.* 461 (1992), a book, *Fundamentals of Corporation Law* (Foundation Press, 1995), and a monograph, *A Practical Guide for Corporate Directors* (National Association of Corporate Directors, 1996). A copy of my resume is attached and incorporated by reference.

2. In December, 1995 and January, 1996 I acted as a consultant to the Governance Committee of the Board

of Directors of Archer Daniels Midland Company (ADM). The Committee, consisting of five independent directors, was created by the Board at its October, 1995 meeting following the Annual Meeting of Shareholders. The Committee was appointed in response to a number of issues that had been raised by shareholders in litigation, in direct communications to the Board before and during the Annual Meeting and in shareholder resolutions proposed for the Proxy Statement. In general, the issues raised by shareholders were related to perceptions that the ADM Board was insufficiently independent of management and lacked the necessary structures to assure effective oversight. These criticisms were echoed in the press. Accordingly, the Committee was charged with conducting a critical review of ADM's corporate governance structures and practices and making recommendations for changes that would reflect the best practices followed by other leading American corporations. To that end, the Committee surveyed the corporate governance structures of other corporations, studied recent changes that other large corporations had adopted and conducted an exhaustive review of the corporate governance literature from conferences and business and academic publications.

3. The Committee's deliberations resulted in the attached Governance Committee Report, which was unanimously approved by the Committee members for consideration by the full Board of Directors at its January 15, 1996 meeting. The Report recommended far reaching changes in the governance practices of ADM, all of which were designed to increase the effectiveness of the Board's independent oversight functions and to move ADM to a leadership position in corporate governance. Among other things, the Report called for a reduction in Board size, limitations on the number of management directors and a commitment to a majority of "outside directors" on the Board and delegation of important oversight responsibilities to committees comprised of a majority of outside directors. The Report was initially presented to

and discussed at a pre-Board meeting on January 14, 1996 (which I attended) and unanimously approved by the Board at its regular meeting the following day.

4. It was recognized that many of the Report's recommendations could not be implemented immediately but would be phased in over time. Several important changes were made in the months immediately following adoption of the Report, however. These included a reduction in Board size from 17 to 12 members as of the October 1996 Annual Meeting, the resignation of all management directors except the Chief Executive Officer, the adoption of a mandatory retirement age for directors joining the board as of the 1996 Annual Meeting and the nomination (and subsequent election) of three new "outside directors."

5. I have reviewed the additional changes in corporate governance procedures that are proposed in Exhibit "A" to the Settlement Agreement. In my opinion, the proposed Settlement will strengthen the 1996 Governance Committee Report's commitment to effective and independent Board oversight by implementing some of the Report's recommendations and enhancing others.

6. Comparing the ways in which the ADM Board operated prior to the filing of these shareholder derivative suits and the manner in which it will operate upon approval of the proposed Settlement, some of the more important changes are as follows:

(i) Inclusion in the By-laws of the principles establishing the basic relationship between the Board and management.

(ii) A majority of the Board will consist of directors meeting a more restrictive and comprehensive definition of "outside director" that meets or exceeds accepted legal standards for director independence.

(iii) A guarantee of direct access by the Board to senior management.

(iv) An extension of the duties of the Audit Committee to include the establishment of effective legal compliance and information and reporting systems. The Audit Committee is required to report regularly on the effectiveness of ADM's policies in these respects. In addition, the Settlement provides for outside independent counsel to advise the Audit Committee for a period of at least three years.

(v) The establishment of separate Audit, Compensation and Nominating Committees to be comprised exclusively of outside directors and a Succession Committee to consist of a preponderance of outside directors.

(vi) The realization of the Governance Committee Report's endorsement of the "lead director" concept by creating the new office of Vice Chairman to be chosen by and from the ranks of the outside directors whenever the office of Chairman of the Board is not held by an outside director.

(vii) The creation of a Governance Committee, consisting of all nonmanagement directors, to review and assess the performance of the Board and its Committees at least annually. The Governance Committee, over which the Vice Chairman presides, will also establish performance criteria for evaluating the Chief Executive Officer and disclose those criteria and results of its evaluation to the shareholders annually.

(viii) The capping of director compensation at not more than $100,000 per year and providing

for payment of at least half of director compensation in ADM shares.

(ix) The encouragement of broader search procedures for new directors by providing that the Nominating Committee for the election of directors at the 1997 Annual Meeting will be restricted to those outside directors who were first elected to the Board after June 25, 1995.

7. Upon approval of the Settlement, the corporate governance policies of ADM will have been completely transformed from those that existed in June, 1995. Whereas ADM's Board of Directors then consisted of 17 members, most of whom had served for many years and many of whom also had management positions, the new ADM Board consists of 13 members with a clear majority of outside directors. Whereas the Chief Executive Officer was then seen to dominate the Board, the office of Chief Executive is now clearly accountable to the Board in fact, as well as theory, and the CEO is the only management director on the Board. The decisive role in the new ADM Board will be played by its outside directors who will consitute both a majority in numbers and the exclusive membership of the key standing Committees of the Board. Through the adoption of a mandatory retirement age and regular self-assessment, ADM's governance structure will also insure against stagnation and complacency in the years to come. The new structure also directly addresses what were perceived to be deficiencies in ADM's communications with its shareholders and other important constituencies. A newly created Public Policy Committee will be responsible for assuring that ADM meets its social responsibilities and for regularly communicating with institutional investors, analysts and others regarding those important issues.

8. While ADM's proposed governance structure reflects the consensus view of best corporate practice, it goes

beyond mere aspiration to establish a workable set of concrete principles that can and will be followed in practice. In my judgment, approval of the Settlement will move ADM to the very forefront of American corporations in terms of corporate governance and mark it as a leader in that field.

/s/ Michael P. Dooley
MICHAEL P. DOOLEY

Sworn to in Albemarle County,
Virginia, this 27th Day of June, 1997. Before:

/s/ Patricia B. Graham
Notary Public
My Commission Expires: August 31, 1997

RESUME

Michael P. Dooley
William S. Potter Professor of Law
University of Virginia
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580 Massie Road
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I. *Personal*

Born, Iowa City, January 16, 1939.

II. *Academic Record*

B.A., Political Science, 1960, University of Iowa; J.D., with high distinction, 1963; University of Iowa; Comment Editor, *Iowa Law Review*, 1962-63; Order of the Coif.

III. *Employment History*

Associate, Dewey, Ballantine, Busbby, Palmer & Wood, New York, New York, 1963-1968.

Associate Professor and Professor, University of Illinois College of Law, 1968-1972.

Visiting Professor, University of Virginia School of Law, 1971-1972; Professor 1972-1980; Henry L. and Grace Doherty Professor 1980-1990; William S. Potter Professor since 1990; Sullivan & Cromwell Research Professor 1992-95.

Visiting Professor, University of Michigan, Summer, 1974; University of Southern California, Summer, 1977; Salzburg Seminar in American Law and Legal Institutions, 1986.

IV. *Publications*

"The Effects of Civil Liability on Investment Banking and the New Issues Market," 58 *Va. L. Rev.* 776 (1972).

"Illiquidity and Exploitation: A Proposed Statutory Solution to the Remaining Close Corporation Problem," 63 *Va. L. Rev.* 1 (1977) (with J. Hetherington).

"Should Management's Control of the Corporation be Weakened and that of the Shareholder Strengthened?" in *The Attack on Corporate America: The Corporate Issues Sourcebook* 82 (M. Johnson ed., McGraw-Hill, 1978).

"Have Delaware's Incorporation Laws Set a Bad Example for Other States?" in *id.* at 145.

"Enforcement of Insider Trading Restrictions," 66 *Va. L. Rev.* 1 (1980).

Controlling Giant Corporations: "The Question of Legitimacy" in *Corporate Governace Past and Future* 28 (H. Manne ed. 1982).

"European Proposals for Worker Information and Co-Determination: An American Comment," in Harmonization of Laws in the European Communities, 126 (Herzog, ed. 1983).

"The First Amendment and the SEC: A Comment," 20 Conn. L. Rev. 335 (Winter 1988).

"The Role of the Board in Derivative Litigation: Delaware and the Current ALI Proposals Compared." 44 *Bus. Law.* 503 (1989) (with E. N. Veasey), reprinted in *The American Law Institute Corporate Governance Project in Mid-Passage: What Will It Mean to You?* (National Legal Center for the Public Interest 1991).

A Practical Guide for Corporate Directors (National Association for Corporate Directors, 1996).

"Two Models of Corporate Governance," 47 *Bus. Law.* 461 (1992).

Fundamentals of Corporation Law (Foundation Press, 1995).

V. *Published Speechs and Remarks*

ABA National Institute, *Dynamics of Corporate Control V: The Sea Change in Corporate Governance and Litigation Issues in the 1990s* (1991).

Symposium: Punitive Damages, 56 So. Calif. L. Rev. 155 (1982).

Business Roundtable/Emory Univerity Law and Economics Center Conference on *Remedies Under the ALI Proposals,* 71 Corn. L. Rev. 357 (1986).

Response to Perkins, *The Genesis and Goals of the ALI Corporate Governance Project,* 8 Gardozo L. Rev. 695 (1987).

Liberty Fund Symposium on *The First Amendment and Securities Regulation,* 20 Conn. L. Rev. 383 (1988).

VI. *Subjects Taught Recently*

Corporate Financial Transactions: Principles and Practice

Corporate Governance and Finance

Mergers and Acquisitions

Contracts

Securities Regulation

Torts

VII. *Miscellaneous*

Director of Graduate Studies

Reporter, ABA Model Business Corporation Act (1996-)

Member, Legal Advisory Committee, New York Stock Exchange Board of Directors (1991-1995)

Member, ABA Committee on Corporate Practice (1995 to date)

Member, ABA Committee on Corporate Laws, (1983-1990) and (1996-)

Member, ABA Corpro Committee (Section Liaison with ALI, Corporate Governance Project) (1984-93)

Member, ABA Task Force on Executive Compensation
Member, Virginia Bar Association Corporate Code Task Force

Chair, Business Law Section, American Association of Law Schools (1986-87), Executive Committee (1981-87)

Ruby R. Vale Distinguished Academic, Widener University School of Law (1996)

Outside Evaluator, George Mason University Law School (1988) (Report prepared for GMU Vice Provost for Academic Progress)

Member of Southern Association Colleges and Schools Reaccreditation Team for Emory University (1993)

Consultant, Attorney General of Virginia and Joint Legislative Audit and Review Committee

Co-Reporter, Virginia Bar Association project to revise the Virginia Stock Corporation Act (1973-74)

Member, ABA Federal Regulation of Securities Committee and Legislation Subcommittee (1974 to 1980)

Member, New York, Illinois and Virginia bars

Lecturer or panelist, numerous bar and academic seminars

October 1996

GOVERNANCE COMMITTEE REPORT TO THE BOARD OF DIRECTORS OF ARCHER DANIELS MIDLAND COMPANY

The Mission of Archer Daniels Midland Company has been to develop a global processing firm that produces high quality food, feed, fuel, and pharmaceutical products from agriculture at the lowest cost possible and in a manner that is responsive to the ethical, legal, institutional, and social priorities of society. The Company's purpose is to add value to raw materials to feed the world. We have succeeded in our mission, and we intend to continue to do so in a way that maximizes shareholder return over time. With the likely doubling of the world's population over the next twenty-five years, we have a special responsibility both to the developing world and the developed world to be the "Supermarket to the World." This is the challenge that we, as a Board of Directors, must shoulder in leading ADM into the next century.

As we look into the next century, we see an opportunity to establish policies and procedures of corporate governance that facilitate our corporate mission. The following principles will guide our actions in the coming years. Succeeding Boards of Directors periodically should review these policies, and the effectiveness of our corporate procedures, to assure that the Company has the governance structures necessary to achieve our goals profitably and responsibly and that the Board remains accountable to the shareholders for its actions.

Principal Duties of the Board.

The Board of Directors is to oversee, not manage, the business and affairs of the Company. The Board should select the Chief Executive Officer and regularly evaluate and appropriately compensate the CEO and senior management of the Company. The Board should develop

and review management succession plans and approve the major strategies and financial objectives of the Company. The Board should provide advice and counsel to senior management, and select and recommend to shareholders an appropriate slate of candidates for the Board of Directors. The Board should periodically review its own performance, its committee structure, the quality of its communications with management, and its handling of critical issues of corporate planning and leadership succession in management and on the Board itself.

Independence of the Board of Directors.

The Board of Directors should have appropriate structures and policies to ensure that the Board acts at all times in the best interests of the Company and its shareholders. The Company looks to outside directors to provide an independent view of the performance of the Company and its management. Accordingly, to assure the highest standards of independent judgment and accountability, a majority of the Board should be comprised of outside directors.

Outside and Nonmanagement Directors Defined. An "outside director" means a director who (a) is neither a current employee nor a former member of senior management of the Company; (b) does not have any personal business or professional relationship with the Company that is material to it or to the director; (c) does not have a close family relationship with any member of senior management; and (d) is not receiving compensation from the Company in any capacity other than as a director. A "nonmanagement director" means a director who is not a current employee of the Company.

Management and the Board. The Chief Executive Officer should be a member of the Board of Directors. In order to assure the greatest number of

outside directors on a board of manageable size, other direct management representation should be kept to a minimum and should, in no event, exceed one or two other management directors.

The Board of Directors should make clear to senior management of the Company that board membership is neither necessary to their present positions nor a prerequisite to a higher management position in the Company. Attendance of management staff at Board Meetings should be at the discretion of the Chairman but should be encouraged by the Board. The Board should have full and direct access to members of senior management and should be encouraged to request reports directly to the Board by any member of senior management. Board members should use judgment in dealings with management so that they do not distract management from the business operations of the Company.

Conflicts of Interest. A director's personal financial or family relationship may occasionally give rise to that director's material personal interest on a particular issue. The Board of Directors should determine whether such a conflict of interest exists on a case-by-case basis. The Board should take appropriate steps to identify such potential conflicts and to assure that a majority of the directors voting on an issue is disinterested with respect to that issue.

Leadership of the Board.

Chairman of the Board. The Board of Directors should decide annually whether it is in the best interests of the Company that the Office of Chairman of the Board and Chief Executive Officer of the Company be separate or vested in the same person.

Lead Director. If the offices of Chairman and Chief Executive Officer are combined in one person,

the outside directors should annually elect one of their number to serve as Lead Director. The Lead Director should preside over all meetings of nonmanagement directors and should perform such other duties and functions as the outside directors may assign. The nonmanagement directors should meet together at least annually, without management present, to evaluate Company performance.

Board Composition.

It is important that the Board include members with the personal qualities and business experience that taken together will assure a strong Board of Directors. The principal qualities of an effective corporate director include strength of character, an inquiring and independent mind, practical wisdom and mature judgment. Special emphasis should be placed on diversity of the Board of Directors. The Board should include members who enable the Company to maintain relationships with customers and other constituencies and to respond to developments in the markets in which the Company operates.

The Board may vary in size and composition as circumstances require. The Board should consist of a minimum of nine members and a maximum of fifteen members. Current nonmanagement directors younger than seventy and new nonmanagement directors should not be candidates for the Board of Directors after reaching their seventieth birthdays. The Board should reduce its current size to reflect a majority of outside directors by the next Annual Meeting, and any interim board member appointment should be made in a manner consistent with these principles.

The CEO should develop an orientation program for new members of the board, including arranging for each new director to meet privately with key members of senior management and to tour the Company's principal facilities.

Evaluation of the Chief Executive Officer.

All nonmanagement directors should participate in the establishment and approval of performance criteria for evaluation of the CEO. The Chairman of the Board of Directors, if separate from the CEO, or the Lead Director, should preside over an annual evaluation of the performance and compensation of the CEO. All nonmanagement directors should participate in the establishment and approval of performance criteria for this evaluation and in the actual evaluation of the CEO. Performance in relation to the established criteria should be used to determine the compensation of the CEO.

Communication with Shareholders.

Primary responsibility for communication with shareholders should rest with the CEO. The CEO should undertake shareholder communications on all matters except board policies, in which matters the Chairman of the Board may be the more appropriate person to handle the communications if the offices of Chairman and CEO are separate. Members of the Board of Directors may, from time to time, be called upon by the Chairman or the CEO to assist in such communications.

Procedures for Meetings.

Board members should plan to attend all board meetings and all meetings of committees to which they have been appointed. Agenda and materials submitted for the information of, or for action by, the Board should be submitted to each member at least ten days in advance of the scheduled meeting, if possible. Similarly, such materials prepared for committee meetings should be distributed to committee members at least ten days in advance of scheduled committee meetings. The Board and its committees should schedule a sufficient number of

meetings to allow them to carry out their responsibilities. Board members should review all materials prior to scheduled meeetings and should be prepared to contribute substantively to each meeting. An individual member is entitled to add to the agenda for board or committee meetings any matter that the director reasonably believes should be on the agenda. Board members are expected to maintain the confidentiality of all materials designated as confidential.

Committees of the Board.

The Board of Directors should select committees of the Board as the need arises. Specific responsibilities of the committees would be assigned but the Board reserves to itself the discretion to disband or to create new committees as circumstances dictate. The Chairman, in consultation with the Nominating Committee, should propose committee chairmen and committee assignments annually for Board approval. Members of the various committees should expect to be rotated to new responsibilities on a three to five year basis.

Current committees are Executive, Audit, Nomination, Compensation and Succession, and Corporate Governance, which should evolve into a Public Policy Committee. All committees except the Executive Committee should be made up of outside directors.

Each committee chairman should determine the frequency, length and agenda for committee meetings. Management should provide, on a priority basis, all information necessary for each committee to carry out its responsibilities. Each committee should report to the Board of Directors at the next meeting of the Board of Directors following the committee meeting. Each committee should have a formal written charter, encompassing at least the major responsibilities described below.

The Executive Committee. The Executive Committee should consist of the CEO and a majority of

outside directors. The Executive Committee is to meet only in those circumstances when a quorum of the Board cannot be convened in a timely manner and the Chairman deems prompt Board action or advice to be in the best interests of the Company, subject to any limitations on the Executive Committee's authority as may be imposed by the Board of Directors.

The Audit Committee. The Audit Committee of the Board of Directors should review the over all plan of independent audit of the Company, the scope of audit procedures, the Company's financial statements, the performance of the Company's independent accountants and internal auditors, and the auditors' evaluation of internal controls. The Audit Committee also should have responsibility to act as liaison between the auditors and management on any areas of material dispute and to discuss with management the Company's major financial risk exposures. The Audit Committee should report at least annually to the Board of Directors on the Company's material litigation risks and significant accounting issues affecting the Company's operations or financial performance.

The Nominating Committee. The Nominating Committee of the Board of Directors should determine the criteria for candidates for the Board of Directors and submit such criteria for full Board approval annually. The Nominating Committee should consider a candidate's skills, technical knowledge, leadership, diverse background and other specific criteria appropriate for the current needs of the Company and consistent with the obligations of board service described in this report. Special emphasis should be placed on diversity of the Board of Directors.

The Nominating Committee should consider any candidate suggested in writing by a shareholder at least one hundred and twenty days prior to the annual meeting when that suggestion is accompanied by appropriate qualifications and a statement signed by the nominee indicating a willingness to serve on the Board of Directors. Upon approval of the Board of Directors, the Chairman of the Nominating Committe should extend invitations to candidates to accept nomination to the Board of Directors.

The Nominating Committee also should undertake the duties of self-assessment and board evaluation described above. Term limits should not be imposed upon any board member, but the Nominating Committee should evaluate the performance during the preceding term of each board member whose renomination is being considered. Board members whose job responsibilities change during the preceding year should advise the Nominating Committee of their changes in circumstances and describe any impact which the changes may have upon their board service.

The Compensation and Succession Committee. The Compensation and Succession Committee should review and recommend to the Board of Directors the annual compensation and benefits of senior management, review new executive compensation programs and evaluate the operation of current executive compensation programs, periodically review policies for the administration of executive compensation programs, and periodically review policies regarding executive perquisites. The Compensation and Succession Committee should review the advisability of a formal plan for an annual or long-term incentive program for senior management. The Compensation and Succession Committee also should be charged with developing, with management, detailed plans of succesion and executive development.

The Public Policy Committee. After its present assignment is completed, the Governance Committee should become a committee of social responsibility designated as the Public Policy Committee. This committee would oversee matters of legal compliance, including issues of potential discrimination, antitrust, foreign corrupt practices act enforcement, and environmental conduct as well as any other issues which have significant social implications anywhere in the world. The Public Policy Committee also should oversee the Company's policies and procedures regarding compliance with the law, and the adequacy of the Company's procedures for circulating these policies, educating all employees regarding these policies, and assuring adherence to these policies by all employees.

Technical Advisory Council.

The Board of Directors encourages the CEO, in his discretions, to create a Technical Advisory Council. The Council would consist of outstanding men and women who are not members of the Board of Directors but whose special expertise in matters related to the Company's business may be helpful to the Company.

Board Compensation.

Each year the Compensation and Succession Committee should review the status of board members' compensation in relation to the practices of similar, large companies and make recommendations for the following year to be considered by the full Board. The level of compensation paid should take into account the responsibilities and risks of board service and should be commensurate with the compensation of directors at similar companies. Compensation should be directed toward tying board performance to Company performance so that board members have a financial incentive to act in the best long-term interests of the Company.

Eligible board members should receive one-half of their compensation in cash and one-half in appropriate forms of stock interests. A portion of the cash compensation should be deferrable at a director's option. The Company should not provide health or retirement benefits to non-management directors by reason of their board service.

Dated: January 15, 1996.

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

[Caption Omitted in Printing]

OBJECTIONS OF CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM AND FLORIDA STATE BOARD OF ADMINISTRATION TO PROPOSED SETTLEMENT OF DERIVATIVE ACTIONS

Preliminary Statement

By Order dated May 30, 1997, the Court invited comments from all shareholders of defendant Archer Daniels Midland Company ("ADM") on a proposed Stipulation of Settlement dated May 29, 1997 ("Settlement") that would, if approved, provide for an award of *as much as $4 million in payments to the plaintiffs' lawyers and experts* (more than half the total cash consideration of the Settlement, with the remainder to go toward *other* lawyers' fees) and the adoption of substandard corporate governance policies that the company, in any event, had for the most part already agreed to adopt.

It is not surprising that the lawyers seek to rush this deal through the Court;[1] it cannot pass careful scrutiny.

[1] The Court, urged by the lawyers who stand to benefit most (if not exclusively) from the proposed Settlement, has provided little time within which the truly interested parties—the shareholders—may object. Under the schedule proposed by the lawyers and approved by the Court, the shareholders had only to July 3, 1997, to lodge their written objections, with the hearing on final approval set for only four days later (July 7). Because the notice of this proposed Settlement was provided to many major holders (such as the shareholders filing the instant objections) only recently, there has not been adequate time for preparation of materials supporting the objections. Accordingly, objectors respectfully request that the Court, at very least, adjourn the hearing for one month so that objecting shareholders may have the opportunity to provide the Court with materials in support of their objections in advance of the hearing, and all shareholders objecting to this proposed resolution may be fully heard. It is settled that objecting shareholders should be permitted a full opportunity to develop a factual record and be allowed meaningful participaton in the hearing. *Bell Atlantic Corp. v. Bolger*, 2 F.3d 1304, 1314-15 (3d Cir. 1993).

It benefits only the lawyers, and at the expense of the ADM shareholders who have already been ill-served by both ADM's board and plaintiffs' lawyers. The Court should derail this speeding (gravy) train. It should insist on careful consideration, after proper notice to shareholders and an *adequate* opportunity for them to submit reasoned objections and materials in support of such objections. Such careful scrutiny will show that what is proposed as a victory for the ADM sharehoders is, in fact, gorging by lawyers in return for acquiescence to unacceptance governance practices.

Interests of the Objectors

Objector California Public Employees' Retirement System ("CalPERS") is the nation's largest governmental ("public") pension fund: it manages assets with a current market value of more than $110 billion on behalf of over one million U.S. citizens who are its employees and beneficiaries. CalPERS currently owns more than 2.8 million shares of ADM stock, and on information and belief is one of the largest single holders of ADM shares.

Objector Florida State Board of Administration ("SBA") is also a large public pension fund, with assets having a market value of over $83.3 billion for the Florida Retirement System Trust Fund, the Local Government Surplus Funds Trust Fund, and other various trust funds on behalf of 586,796 employees and 149,571

current beneficiaries. SBA currently owns 1,765,977 shares of ADM stock.

Objectors CalPERS and SBA are, on information and belief, the largest ADM shareholders that have taken any public position on the proposed Settlement.

Lawyers for the nominal plaintiffs contacted the Council of Institutional Investors ("Council")—a prominent organization of large institutional shareholders, whose members control more than $1 trillion in assets—regarding this litigation. CalPERS and SBA, who are both members of the Council, informed ADM that major shareholders would object to the proposal as inadequate and unfair to ADM shareholders, for the reasons stated in this memorandum. ADM has ignored these objections and instead has pressed forward for Court approval of the proposed Settlement. *See* Declaration of Ann L. Yerger ("Yerger Decl.") ¶¶ 9, 10.

Argument

THE PROPOSED SETTLEMENT SHOULD BE REJECTED AS INADEQUATE AND UNFAIR TO THE SHAREHOLDERS OF ADM

It is a matter of public record that the management of ADM as been accused of, and has admitted culpability to, grave misconduct. *See* Declaration of Steven F. Benz ("Benz Decl."), Exhiabits B - J (collecting press reports of ADM plea and settlement agreements). The instant lawsuit was filed, ostensibly, to provide redress to the corporation and its shareholders. Counsel for the nominal plaintiffs [2] claimed that ADM suffered more than

[2] As is typically the case in a derivative action, nominal plaintiffs here have little if any demonstrated interest in the litigation. There is no indication that they hold a substantial number of ADM shares —in contrast to the substantial holdings of objectors CalPERS and SBA. As many courts and commentators have noted, it is the lawyers and not the plaintiffs who effectively function as the parties

$190 million in damages as a result of the misconduct alleged in the complaint,[3] and acknowledged in writing to the Council of Institutional Investors that "a primary goal of our litigation is to recover for ADM as much of the wasted $190 million as is realistically and reasonably possible . . . ." Yerger Decl., Exhibit A. Counsel also vowed to install effective governance provisions that would prevent further misconduct. *Id.*

But since the action was filed, virtually nothing has been done to achieve those goals. After defendants filed a motion to dismiss, pursuant to Fed. R. Civ. P. 12(b)(6), it appears that the case became dormant. No motions were litigated (including the Rule 12(b)(6) motion); discovery soon reached impasse, if it ever began. *See* Settlement at 4-5.[4]

in a derivative action. *E.g., Bolger*, 2 F.3d at 1309 (in derivative actions "the client, as principal, is neither well-situated nor adequately motivated to closely monitor and control the attorney"); K. Winter, *Paying Lawyers, Empowering Prosecutors and Protecting Managers: Raising the Cost of Capital in America*, 42 Duke L.J. 945, 948 (1993) (in derivative actions named "plaintiffs are generally figureheads"); John C. Coffee, Jr., *Understanding the Plaintiff's Attorney: The Implications of Economic Theory for Private Enforcement of Law Through Class and Derivative Actions*, 86 Col. L. Rev. 669, 677-78 (1986) (in derivative actions "the actual client generally has only a nominal stake in the outcome of the litigation" and cannot closely monitor and control the attorney's conduct).

[3] Plaintiffs' expert, Mr. Miller, opines that the damages far exceed $190 million, and that a conservative estimate would be $250 million or more. *See* Declaration of R. Alan Miller ("Miller Decl.") ¶ 11.

[4] Objections are unable to determine, from the Settlement and related pleadings what, if any, discovery counsel claim to have done, since they make no reference to any specific discovery taken. The Court's docket sheet, moreover, reflects only that a motion to dismiss was filed—and never ruled upon, and that there were motions to compel discovery that, with consent of the lawyers, were deferred no less than *seven* times and ultimately never ruled on. Benz Decl., Exhibit A (Civil Docket for Case No. 95-CV-2279).

Having done little but wait, the lawyers then entered into what can only be characterized as a sweetheart deal with defendants: Defendants obtain Court-sanctioned releases for virtually all of their misconduct in return for (1) payment of a total of $8 million (with up to 49 percent of this—and perhaps more, if interest is included—earmarked for the attorneys), Settlement at 15; and (2) adoption of a diluted set of "corporate governance" principles that not only lag behind those of ADM's corporate peers but improve little if at all on reforms that were agreed upon prior to, and independent of, the Settlement. *Id.* at 13.

Under the settled standards of Rule 23.1 for judicial review of proposed settlements (Point I, *infra*), this Settlement cannot possibly pass muster. First, the Settlement provides virtually all of its benefits to the *attorneys* for the nominal plaintiffs. (Point II, *infra*). Second, the supposed jewel of the proposed Settlement—the exalted governance principles—are neither jewels nor the fruits of the lawyers' labor. These principles, which are substantially weaker than those now routinely adopted throughout corporate America, were for the most part implemented by ADM long before the Settlement was reached. (Point III, *infra*).

Moreover, the proposed Settlement represents a squandered opportunity to enact truly meaningful governance for ADM—a company perhaps more in need of it than any other public company in the United States. Close to half of the ADM shareholders voted for rigorous and meaningful standards of director independence at the last annual meeting. The lawyers' willingness to settle for watered-down rules, in what appears to be *quid pro quo* for enormous and unjustified fees, strongly suggests that the Settlement was collusive and is not in the shareholders' best interests.

In any event, the unseemly rush to approval should be halted; if the Court does not reject it outright, the Court's

obligation under Rule 23.1 to conduct an informed and independent review of the proposed Settlement, and to hear the objections of shareholders who have only recently been informed of this resolution, require the deferral of any final decision to approve the Settlement until after all interested parties have been provided with an appropriate opportunity to present their objections, and materials supporting the objections, to the Court. Since this opportunity has not yet been provided, and the scheduled hearing (on July 7) will not provide the shareholders with a fair opportunity to contest this unfair proposal, the Court should defer the hearing for at least one month.

I. THE COURT MUST EXERCISE INDEPENDENT JUDGMENT TO DETERMINE WHETHER THE PROPOSED SETTLEMENT IS FAIR

Under Rule 23.1, the "action shall not be dismissed or compromised without the approval of the court . . . ." "Under FRCP 23.1, the court has a duty to determine whether the settlement reasonably protects the interests of the corporation and its shareholders." *In re Oracle Sec. Litig.*, 829 F. Supp. 1176, 1179, 1186 (N.D. Cal. 1993), *citing Mathes v. Roberts*, 85 F.R.D. 710, 713 (S.D.N.Y. 1980). In reviewing a proposed settlement of a derivative action, "[t]he generally accepted standard is that the agreement must be fair and adequate in light of the interests of all the parties." 7C C. Wright, A. Miller & M. Kane, *Federal Practice and Procedure* § 1839 at 182 (1986 & Supp. 1997). Before approving the proposed Settlement, the Court "must consider its fairness, reasonableness, and adequacy." *Moore's Federal Practice 3d* § 23.1.10[2][a] at 23.1-58 (1997).

The Court "must also ensure that there are no fraudulent or collusive features of the settlement." *Id.* ("Derivative actions pose the inherent risk that the representative plaintiff will collude with the defendant to forego the

derivative claims in exchange for a settlement that is only favorable to the representative plaintiff and his or her attorneys."); Wright, Miller & Kane, *supra,* § 1839 at 182-84 ("Settlement proposals . . . that do not appear to have been reached as the result of arms length negotiations . . . will not be approved."); *id.* at 191 ("the court should be on the lookout for signs of bad faith or collusion among the parties to the proposed compromise"). As Mr. Coffee has observed, many derivative actions result in settlements that "benefit[] the attorneys more than the shareholder." John C. Coffee, Jr., *Understanding the Plaintiffs Attorney: The Implications of Economic Theory for Private Enofrcement of Law Through Class and Derivative Actions,* 86 Col. L. Rev. 669, 673 n.9 (1986).

The burden here is entirely on the proponents of the Settlement. "The proponents of the settlement have the burden of proving that the settlement is in the best interests of the corporation." *Moore's Federal Practice 3d, supra,* § 23.1.10[2][a] at 23.1-58. It is the plaintiffs' attorneys who must therefore prove the fairness and adequacy of the proposed settlement. Wright, Miller & Kane, *supra,* § 1839 at 184-86 ("The burden is on the proponents of the compromise to show that it meets this standard, and the trial court should state its reasons for deciding to approve a settlement so as to provide adequate information for appellate review.").

Held to this exacting standard, the proposal here cannot possibly be found fair, reasonable and adequate in its benefits to ADM and its shareholders.

II. THE SETTLEMENT SHOULD BE REJECTED BECAUSE IT PROVIDES EXCESSIVE BENEFITS TO THE NOMINAL PLAINTIFFS' ATTORNEYS

The total cash consideration achieved in the proposed Settlement is $8 million. Settlement at 12-14. Of that

$8 million, up to 49 percent (more, in fact, if interest is included) is earmarked for payment to the attorneys for nominal plaintiffs. *Id.* at 15. The remainder of the cash is to be used for payment to "outside independent counsel" employed in some vague capacity to assist the ADM board members in discharge of their legal responsibilities. Settlement at 5 & Exhibit A.

There is, accordingly, *no* benefit to the shareholders from the cash portion of the proposed Settlement. It appears that at least half will be paid directly to the plaintiffs' attorneys, as reward for their (non) prosecution of the action; the rest will be used for more lawyers, presumably to remind the ADM directors of their obligation to follow the company's bylaws and other legal requirements. No benefit to ADM or its shareholders is seriously posited from these payments, nor can any legitimate benefit plausibility be put forward. The only real beneficiaries of the arrangement, stated bluntly, are the lawyers. It is axiomatic that settlements provided excessive benefits to the lawyers cannot be approved under Rule 23.1. *E.g., Rosenbaum v. MacAllister,* 64 F.3d 1439, 1443-48 (10th Cir. 1995) (rejecting under Rule 23.1 disproportionate settlement benefitting attorneys); *In re Pittsburgh & Lake Erie R.R. Co. Sec. and Antitrust Litig.,* 543 F.2d 1058, 1070 (3d Cir. 1976) (rejecting settlement where disproportionate cash benefit to plaintiffs' lawyers); *see also* Wright, Miller & Kane, *supra,* § 1839 at 184-85 n.26 (collecting cases under Rule 23.1 in which settlements have been rejected for this reason).

The results do not warrant the excessive fees sought. Plaintiffs seek the Court's approval of a settlement that provides virtually no cash benefit to the corporation—it all goes to the lawyers. The only purported benefit, enactment of supposed "corporate governance" principles, resulted *not* from plaintiffs' efforts but rather from the recommendation of the ADM board's Governance Committee. *See* Point III, *infra.* Moreover the ADM principles fall far short of effective governance. Indeed, they

fall far short of the effective and independent director standards that 41.6 percent of the ADM shareholders voted to approve at ADM's October 17, 1996 Annual Meeting. *See* Declaration of Sarah A.B. Teslik ("Teslik Decl.") ¶ 10. Plaintiffs' lawyers *directly acknowledged* that the Settlement's governance principles were selected precisely because they would not require ADM to change its board *at all*. Yerger Decl. ¶¶ 9, 10.

The effort expended does not justify the excessive fees. The attorneys' own summary of the proceedings to date proves that they have done little, if anything, to prosecute the case.[5] After the filing of defendants' motion to dismiss, they appear to have let the matter sit in suspense despite the known interest of many of ADM's largest shareholders. These holders individually and collectively through the Council offered to assist in the prosecution of the case (and specifically to help structure necessary governance reform). When the Council provided comments to these attorneys, the Council's comments were largely ignored.

According to the lawyers, they can point only to

> consulting with experts in the areas of corporate governance and economics, and with the company's largest institutional investors, and reviewed and analyzed treatises, articles, and authoritative reports on corporate governance issues. In addition, Plaintiffs' counsel reviewed and analyzed thousands of pages of documents produced by defendants, reviewed and analyzed the Company's public filings and press releases, and thoroughly analyzed and evaluated the facts supporting Plaintiffs' claims.

Settlement at 4-5. Perusal of papers and hiring expensive experts aside, it is apparent that the lawyers—who seek up to $4 million in fees—did little to prosecute the action, which may explain why so little of value was achieved notwithstanding defendants' public admissions of wrongdoing. The Court should be leery of approving a settlement where, as here, little if any discovery was done to determine whether plaintiffs were likely to succeed on their claims. *See Bolger*, 2 F.3d at 1314 ("post-discovery settlements are more likely to reflect the true value of the claim and be fair").

The excessive fees support an inference of collusion, and at very least require full and careful consideration by the Court before any approval. That all of the settlement cash has been earmarked for lawyers calls into question the legitimacy of the proposed Settlement. Large payouts to lawyers, coupled with purely spectral, supposed "structural" benefits to the corporation, are harbingers of collusion.[6] In similar circumstances fee claims have been far less. A 1991 study, for example, found that the average fee award in "structural relief" shareholder cases was

[5] In preparing this objection CalPERS and SBA have been hampered by the unduly cramped schedule imposed on the Court by counsel for plaintifis. They have been required to submit their objections, and to divine the basis for what appears on its surface to be excessive benefits for the attorneys, without adequate time to review the fee petitions of the lawyers—which were filed only two days before all written objections had to be filed with the Court. *See* Order Preliminarily Approving Settlement and Providing for Notice, ¶¶ 7, 9 (May 30, 1997). With this impossible schedule, objectors plainly were not given adequate time to prepare and submit their objections to the proposed Settlement and the lawyers' claims to the lion's share of that Settlement. This alone requires deferral of any action by the Court save outright rejection of the proposed Settlement.

[6] Courts and commentaries have recognized that "[o]ne of the risks flowing from shareholders' difficulty in monitoring derivative litigation is that plaintiffs' counsel and the defendants will structure a settlement such that the plaintiffs' attorneys' fees are disproportionate to any relief obtained for the corporation. Plaintiffs' attorneys and the defendants may settle in a manner adverse to the interests of the plaintiffs by exchanging a low settlement for high fees." *Bolger*, 2 F.3d at 1310. "At its worst, the settlement process may amount to a covert exchange for a high award of attorney's fees." Coffee, *supra*, n.2 at 714.

$287,000. Roberta Romano, *The Shareholder Suit: Litigation without Foundation?*, 7 J.L. Econ. & Org. 56, 63 (1991).[7]

Objectors are thus confronted with the stark fact of the lawyers' huge fee demand, unsupported by any facts. At the very least, objectors and other shareholders who may, with adequate notice, choose to object should be afforded a reasonable opportunity to contest this highly suspect resolution.

Accordingly, if the Court does not reject outright this proposed Settlement—as it should, in light of the plainly excessive benefits to the attorneys—it should defer consideration of the Settlement until after all shareholders have been afforded a reasonable opportunity to be heard, with sufficient advance notice to permit them to study all of the relevant materials (including the lawyers' fee petition) and to submit materials supporting their objections sufficiently in advance of such hearing to permit the Court to consider them fully.

III. THE AGREEMENT BY ADM TO ADOPT CERTAIN "GOVERNANCE" PRINCIPLES PROVIDES NO BASIS TO APPROVE THE SETTLEMENT

As the court observed in *Bolger*, "it is difficult to assess the substantive fairness of nonmonetary settlement relief." 2 F.3d at 1314. Such claimed "structural" relief "may be used to mask an unfair settlement that benefits individual defendants and plaintiffs' counsel but not the corporation." *Id.* But no such difficulty is present here, for

[7] The average fee award in "monetary" settlement cases was higher, but still only came to $1.45 million. *Id.* The study also found that in monetary settlement cases, fee awards averaged not more than *24 percent* of the monetary settlement. *Id. See also* 3 Herbert B. Newberg & Alba Conte, *Newberg on Class Actions* § 14.03, 14-13 to 14-14 (3d ed. 1992) (discussing attorneys' fees in securities and antitrust suits as ranging from 20 to 30 percent).

the non-monetary benefits supposedly achieved in the Settlement are nothing more than the same supposed "reforms," inadequate as they are, that the company adopted more than a year ago.

ADM has long been a poster-child for advocates of effective corporate governance, and most pointedly for those—such as the Council—who seek boards of directors independent of the company's management. Yerger Decl. ¶ 11.[8] Much of ADM's current troubles, in the view of objectors, can be traced to the defendant directors' longstanding blood, personal, professional and financial connections to the company's former CEO.[9]

Nothing in the proposed Settlement, however, solves that problem. Or more precisely, the proposed Settlement advances the cause of effective governance not at all beyond what the company had previously agreed to do, and nowhere near principles that require the ADM board to be comprised of truly effective and independent directors.

What ADM agreed to do prior to the proposed Settlement. On January 15, 1996, in response to the demands of its large institutional shareholders and after waves of negative publicity regarding a panoply of corporate mis-

[8] Richard Koppes, CalPERS' former deputy executive director, stated that the ADM Board, perhaps more than any other company, needs a majority of "truly independent directors." Greg Burns, *A Grain of Activism at Archer Daniels Midland*, Business Week, Nov. 6, 1995, at 44. For years, D. Andreas and ADM have ignored the critics of their insider-dominated board. CalPERS, prior to the October 19, 1995 annual meeting, gave ADM the grade of "F" for its failure to respond to CalPERS corporate governance queries. *Id.*

[9] Directors are responsible for formulating corporate policies and monitoring the activities of management in implementing these policies. Employment, business and family relationships can raise conflicts of interest that may limit the vigilance and diligence of the board. It is in the best interest of all shareholders that a majority of board members be independent "outside" directors.

deeds, the ADM board's Governance Committee issued a report, *Governance Committee Report to the Board of Directors of Archer Daniels Midland Company* (Jan. 15, 1996) ("Report"), which was thereafter adopted in its entirety by the entire board. Teslik Decl., Exhibits C and E. The Report purported to set forth enhanced principles of corporate governance, including proposals purporting to provide for independent directors and safeguards against further depredations by management. *Id.*

ADM shareholders seek the adoption of standards for truly independent directors. In view of objectors, and many other ADM shareholders, the recommendations of the Report did not in fact provide for truly independent directors. ADM's proposed principles allowed persons having substantial financial ties to ADM, and hence lacking independence, to serve as "independent" directors. Yerger Decl. ¶ 10.

To remedy this material defect, objecting shareholders (including CalPERS and SBA) submitted a proposal for vote at the 1996 ADM annual shareholders' meeting. This proposal, which received 41.6 percent of the votes over management opposition, provided that no one with any non-trivial personal or financial interest in ADM could serve as an "independent" director. Teslik Decl. ¶ 10.[10] This definition of "independence," notwithstand-

[10] Under this definition, an independent director is one who:

- has not ben employed by the company or in an affiliated executive capacity within the last five years;
- was not, and is not, a member of the corporation or firm that is one of the company's paid advisors or consultants;
- is not employed by a customer, supplier or provider of professional services to the company;
- has no personal services contract with the company;
- is not employed by a foundation or university that receives grants or endowments from the company;
- is not a relative of the managemnt of the company;

ing widespread support, was not adopted by ADM. Any standard that falls short of it, however, permits interested persons to serve as purportedly independent outside directors, and is no safeguard against the sort of crony-board that has characterized ADM for decades. *Id.* ¶ 9.

The proposed Settlement does not add to the reforms adopted based on the Report. In substance, the proposed governance principles included in the Settlement no more than track the elements of the program adopted in the Report. *See* Teslik Decl. ¶¶ 8, 11, 12, 13 & Exhibit D. They are, in any event, little more than "prudent safeguards any major corporation should have in place without the impetus of a lawsuit." *Rosenbaum,* 64 F.3d at 1446. In those few areas where the Settlement purports to provide *new* requirements, they are of little or no value in the view of institutional shareholders; they appear to be written to seem meaningful when in fact they are gutted by 'fine-print' qualifiers. Teslik Decl. ¶¶ 8, 9.

Most fundamental, however, is the failure of the proposed Settlement to provide the reform sought by almost half of the shareholders at the last meeting: truly independent directors. Under the definition of "outside" or independent director contained in the proposed Settlement, just as in the Report, a director is considered an "outside" director even if he or she has a personal, business or professional relationship with the company, so long as the relationship is not "material" to ADM or to the director. *Virtually no* relationship *any* one human being can have with a big company can *ever* be material *to the company*. This qualifier thus makes the whole definition meaningless. The proposed Settlement falls far short of the effective reform urged by objectors and other major institutional shareholders. And when a company

- is not an officer of a company on which the company's chairman or chief executive officer is also a board member.

See Teslik Decl. Exh. A (Council's analogous "Definition of an Independent Director").

lacks an independent board, all other governance procedures become meaningless. Teslik Decl. ¶ 9.

In light of its failure to address the pivotal issue of independence, the proposed Settlement's few tinkerings with the proposals already adopted in the Report cannot fairly be said to represent any increased value for shareholders. *Id.* ¶ 15 and Exhibit D (comparing in detail the Settlement provisions with the Report provisions). The few changes added by the proposed Settlement are trivial in comparison to the standards of independence that plaintiffs *did not* obtain.

For example, the adoption of confidential voting (meaning those running for company office cannot count the votes) has only surface appeal. Under the proposed Settlement, there will be confidential voting only where it *will not matter*. In other words, there will only be confidential voting when shareholders can't vote against directors—and no confidential voting in contested situations. As a result, this "reform" is entirely without value.

In support of their claim to have added value through corporate governance enhancements, plaintiffs offer only the conclusory affidavits of their paid experts. Neither expert provides persuasive support for the claim that the proposed Settlement—as opposed to the reforms to which ADM had already agreed in the Report—adds substantial value for the shareholders.

Indeed, plaintiffs' two hired experts focus on *all* of the changes in ADM's corporate governance, rather than on *any* changes specifically extracted by plaintiffs in the Settlement. Teslik Decl. ¶ 16. Most of the claimed governance improvements, however, were achieved without refernece to this action. *Id.* ¶ 11, Exhibit D. Moreover, in important respects plaintiffs' experts are simply wrong. *E.g.* Coffee Aff. ¶ 7 (claiming independence provisions of proposed Settlement mirror those of Council, when in fact they do not). Mr. Coffee simply glosses over the critical role of director independence, and he fails even

to address the respects in which ADM's policies fail to provide for independence.

The Court cannot, on the record before it, conclude that ADM shareholders will be afforded substantial benefits through the proposed Settlement because of the supposed enhancements of ADM's corporate governance. The Court should reject the proposed Settlement as it now stands. At the very least, the Court should require the parties to show cause why these corporate governance provisions should not be revised to include provisions appropriately tailored to achieve genuine independence for outside directors. And in no case should the Court approve the proposed Settlement, as presented, until after a reasonable opportunity for the objectors to participate in a full hearing on the merits of the supposed enhancements to ADM's corporate governance.

Conclusion

The Court should reject the proposed Settlement as inadequate. In the alternative, the Court should adjourn the hearing on the approval of the proposed Settlement, for at least a month, to permit objectors and other sharefor at least a month, to permit objectors and other shareholders similarly situated to participate meaningfully through submission of briefs and other materials in advance of the hearing, by presentation of testimony at the hearing, and through cross-examination of the witnesses (if any) called in support of the proposed Settlement.

Respectfully submitted,

[Listing of Counsel Omitted]

Date: July 2, 1997

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

[Caption Omitted in Printing]

DECLARATION OF ANN L. YERGER

Ann L. Yerger hereby declares pursuant to 28 U.S.C. § 1746:

1. I am over eighteen years of age and have personal knowledge of the matters stated herein.

2. I am currently employed by the Council of Institutional Investor's [*sic*] (the "Council") as director of the Council's research service. The Council is located at 1730 Rhode Island Avenue, Suite 512, Washington, D.C. 20036. The Council is an association of more than 100 public corporate and union pension funds, with more than $1 trillion in assets. I have been employed by the Council since January 1996. Prior to that I was employed for five years by the Investor Responsibility Research Center as Deputy Director of the Center's Corporate Governance Service.

3. On November 5, 1996, Jacob A. Goldberg of the law firm Spector & Roseman, P.C., called me at the Council of Institutional Investors to describe the Archer Daniels Midland Company derivative litigation. I discussed Council members' ongoing concerns about the independence of ADM's board of directors.

4. About a month later, Mr. Goldberg phoned to set up a meeting with the Council. In response to my request for a written summary of the lawsuit, he mailed a letter dated December 15, 1996 to the Council's offices. A true

and correct copy of this letter is attached hereto as Exh. A.

5. In this letter, Mr. Goldberg stressed that the firm was interested in meeting with the Council and Council members to discuss "the troublesome systemic problems plaguing the ADM Board of Directors." Exh. A at 1. A primary goal of plaintiffs' lawsuit, according to Mr. Goldberg, was to "recover for ADM as much of the wasted $190 million as is reasonably and realistically possible from the culpable officers and directors." *Id.* at 2. Equally important, he continued, were "the structural problems with ADM's board." *Id.* Goldberg stated that "any resolution of this case requires us to seek various fundamental changes to the ADM board, its structure and the way [it] governs ADM." *Id.*

6. On December 19, a Council staffer spoke with Mr. Goldberg and Robert M. Roseman of Spector & Roseman, P.C. The Council forwarded its Bill of Rights and definition of "independent" director to the law firm of Spector & Roseman, P.C.

7. That was the Council's last substantive conversation about the lawsuit with counsel for plaintiffs. On May 30, a reporter from the *Wall Street Journal* called me to discuss the proposed settlement. Shortly thereafter, on June 3, an irate individual shareholder faxed a copy of the proposed settlement to the Council.

8. I analyzed the proposed settlement and determined that it makes no meaningful improvement in ADM's corporate governance, and, in my opinion, is not in the best interest of ADM or its shareholders. Most importantly, the proposed settlement's definition of "outside" (or independent) director falls significantly short of the Council's definition. While purportedly modeled after the Council's standard, the proposed settlement's definition added undefined "materiality" hurdles to various categories of "outside" directors that falsely classify "inside" directors as "outside" directors.

9. I immedately contacted Mr. Roseman to explain the Council's concern with the proposed settlement definition and to clarify the impact of the materiality hurdles. In response to my criticism of the proposed definition, Mr. Roseman told me that ADM refused to accept the Council's more stringent definition of "outside" director. He explained that, under the Council's definition, the company would be forced to remove certain directors from its board.

10. I asked Mr. Roseman to provide a written analysis of ADM's board using the proposed definition. Mr. Roseman's response is attached hereto as Exh. B. According to Mr. Roseman's analysis, the only ADM directors who do not qualify as "outside" directors are company chairman Dwayne Andreas, CEO G. Allen Andreas and Shreve Archer, father of ADM's treasurer. All of the remaining 10 board members qualify as "outside" directors under the proposed settlement's definition, even though four directors—two attorneys whose law firms provide legal services to the company, and two executives of companies or their affiliates that do business with ADM—have ongoing business relationships with ADM and accordingly are beholden to management. These four directors do not qualify as independent "outside" directors under the Council's definition or any other generally accepted standard of true independence.

11. ADM has been a poster child for the corporate governance movement for years. The settlement of this derivative action offers an unprecedented opportunity to implement changes in ADM's bylaws that will benefit ADM and its shareholders. This opportunity should not be squandered.

12. I do not believe that the proposed settlement is fair, reasonable, adequate, or in the best interest of ADM and its shareholders. Indeed, I do not believe that the proposed settlement offers any significant benefit to ADM or its shareholders.

I declare under penalty of perjury that the foregoing is true and correct.

Dated this 2d day of July, 1997.

/s/ Ann L. Yerger
ANN L. YERGER

[Notarization and Exhibits Omitted in Printing]

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

[Caption Omitted in Printing]

DECLARATION OF SARAH A.B. TESLIK

Sarah A.B. Teslik hereby declares pursuant to 28 U.S.C. § 1746:

1. I am over eighteen years of age and have personal knowledge of the matters stated herein.

2. I have been the Executive Director, attorney and principal staffer for the Council of Institutional Investors (the "Council") since its formation in 1985. The Council is a non-profit association of corporate, public and Taft-Hartley pension funds that addresses investment issues. Council members invest over a trillion dollars on behalf of millions of employees and beneficiaries. Objectors California Public Employees' Retirement System and the Florida State Board of Administration are members of the Council.

3. The Council is a very deliberate and cautious organization that only adopts policies on essentially unanimous votes, and only after careful research and discussion. The Council has adopted fewer than a dozen corporate governance policies in all of its years of existence. Each of these has been so basic that every one of the Council's corporate members has voted in favor of each of the policies put up to them for a vote, and most of the policies are standard operating procedure at most or many of the nation's largest companies.

4. The first and probably the most central of the Council's policies is its requirement that a majority of a corporation's directors be independent from potentially compromising financial, familial or professional relationships to the company. The Council defines independence for these purposes in a detailed definition which, in essence, defines a director as independent if his or her only non-trivial connection to the board is his or her board seat. Members adopted this definition after they agreed that a board was much less likely to perform properly its central function as an independent oversight body if most of its individual members were not, in fact, independent. Without this foundation policy, members felt most other corporate governance standards and procedures were meaningless. The policy and definition were adopted with unanimous votes on April 5, 1991. A copy of this policy is attached hereto as Exhibit "A".

5. The other central policy of the Council is its position on confidential voting. Directors, of course, are elected by shareholders, and so the election process is the vital link that provides meaningful accountability to shareholders. When this policy was debated, members agreed unanimously that this link is weakened, threatened, or shattered if those who run for office count their own ballots. That is an election practice that members did not believe would be tolerated in any other part of American life and should not be tolerated in corporate elections either.

6. The Council therefore on June 23, 1989 unanimously adopted a policy, attached hereto as Exhibit "B", supporting a confidential ballot—supporting the idea, in other words, that neutral third parties selected by the corporation should count shareholders' proxies. With increasing numbers of employee and institutional service provider shareholders who could suffer retribution if they dared to cast votes against management, members believed that this policy would only become more important over time.

7. The Council's majority standard for board independence is so universally accepted that it is the standard now used by nearly 85 percent (84.7 percent) of S&P 500 companies. Indeed Council data indicate that only 17 companies of the 483 member of the S&P 500 surveyed by the Council have fewer independent directors than ADM.

8. In the proposed settlement ADM offers an independence standard and definition that are, in my opinion (a) completely meaningless because of clever modifying language; (b) virtually identical to changes already proposed by the company more than a year ago, and without reference to the derivative lawsuit; (c) worse (less protective of shareholders) than the standards already in place at all but 15 percent of S&P 500 companies; and (d) so completely dated in language as to be archaic.

9. The proposed settlement provides that directors will be deemed to be "outside" even if they have personal, business, or professional ties to the company and/or its senior management, unless the relationship is deemed by the company to be "*material to the company or to the director.*" With a company the size of ADM, I cannot imagine a single relationship any one person could ever have, personal, professional, or otherwise, to ADM that would be material *to ADM*. This standard is therefore, in my opinion, a standard that virtually no director can fail. And yet it was Council members' belief that even the smallest of financial or personal relationships can genuinely affect a person's independence because of its potential to affect *the person.*

10. The company offers this can't-fail-to-be-met standard despite the fact that the widely accepted Council standard was already submitted to it by two of its largest shareholders, and two of the largest Council members—the California Public Employees' Retirement System and the Florida State Board of Administration—and received an exceptionally high endorsement of 41.6 percent of

voting shareholders at the company's October 17, 1996 annual meeting.

11. The offer in the proposed settlement that direct management representation on the board will be limited to no more than three seats was lifted almost verbatim from the *Governance Committee Report to the Board of Directors of Archer Daniels Midland Company* (Jan. 15, 1996), which is attached hereto as Exhibit "C". This Committee was established and acted prior to the filing of the lawsuit to which this proposed settlement is the proposed conclusion. The ADM board adopted all of the recommendations in the Report. *See* Exhibit "E". So shareholders gain nothing from this proposed settlement they did not already have. And they did not have anything innovtaive here in any event: according to Council data, this company suggestion is standard operating procedure at most S&P 500 companies anyway—86.5 percent have three or fewer executives on the board.

12. Similarly the concept of a "lead director" seems to me to be another essential repeat of a change already called for in the 1996 Report, with the renaming of the lead director as the vice chairman. A similar repackaging appears to have occurred with the the settlement's proposal to establish a governance committee to assess board and committee effectiveness. Under current board policies the nominating committee is responsible for annual director "self-assessment and board evaluation," while all nonmanagement directors handle the "establishment and performance criteria for evaluation of the CEO." As a result, the creation of this separate corporate goverance committee does not appear to represent any meaningful innovation from current company practice.

13. The proposed settlement's requirement that separate nominating, compensation and audit committees must be composed exclusively of outside directors was also lifted verbatim from the 1996 Report.

14. The proposed settlement does offer a version of confidential voting that was not contained in the Report. But it is, if anything, an even more meaningless provision, in my opinion, than the definition of independence used for directors. The proposed settlement indicates the company will grant shareholders confidential voting—but only, it seems, in those situations in which it is irrelevant —only in situations where there are no proxy contests or solicitations. In these situations the proposed settlement indicates there will *not* be confidential voting. And, although it seems nearly irrelevant under the circumstances, the company also does not indicate whether in those trivial and routine situations in which votes will be tallied confidentially, the confidentiality will last only until the polls are closed or whether it is permanent. Other companies with confidential voting policies generally, in the Council's experience, make this clear—it is a distinction that matters a great deal, especially to individual employee shareholders.

15. I have compared the governance provisions of the proposed settlement with the provisions already accepted by the board in the 1996 Report. This comparison is summarized in Exhibit "D" hereto. In my opinion, the few items in the settlement that cannot be found in the Report are trivial and provide no benefit to shareholders. On balance, the proposed settlement is no improvement over the governance provisions already accepted in the Report. I am unable, therefore, to identify new, positive, and meaningful corporate governance changes offered in the proposed settlement. This is particularly surprising and disappointing since I personally, numerous Council members individually, and other members of Council staff repeatedly made offers to ADM directors, consultants and other representatives to provide information on independent directors and other core member and Council policies that could have formed the basis of a very limited and conservative but meaningful set of governance principles.

16. Since the proposed governance provisions offer nothing significantly new, the proposed settlement provides no value to ADM or to its shareholders. However, a *truly* independent board could add significant value. A recent study by the McKinsey & Co. consulting firm found that 50 money managers representing $850 billion in assets were willing to pay an 11 percent "good governance" premium. A discussion of this study is attached hereto as Exhibit "F".

I declare under penalty of perjury that the foregoing is true and correct.

Dated this 2d day of July, 1997.

/s/ Sarah A.B. Teslik
SARAH A.B. TESLIK

[Notarization and Exhibits A-E Omitted in Printing]

EXHIBIT F TO TESLIK DECLARATION

THE WALL STREET JOURNAL, MONDAY, JUNE 30, 1997

WHY INVESTORS PUSH FOR STRONG CORPORATE BOARDS

Manager's Journal
By Jennifer H. van Heeckeren

Trustees and staff of the California Public Employees' Retirement System are developing guidelines to grade companies in Calpers's portfolio on the independence of their boards. Calpers cannot be ignored: Its $80 billion in equities make it one of the nation's largest shareholders and a force to be reckoned with in the governance arena. A study I conducted with Diane Del Guercio at the University of Oregon shows that Calpers has the power to provoke significant change, such as takeover attempts, turnover, restructurings and asset sales.

CEOs would be wise to embrace the idea of strongly independent boards. For if investors can't get boards to work well, they may turn to other measures—sitting on boards themselves, lobbying for direct government regulation or supporting a return of corporate raiders.

The growing power and independence of boards reflects a reversal of a trend that dates to the early years of this century. A seminal event occurred in 1914, when representatives of J.P. Morgan resigned from 30 company boards in a single day. They and other institutional investors had held sway in boardrooms for more than two decades, leaving CEOs with little real decision-making power. But as they came under critical public and political scrutiny, they beat a hasty retreat. Family owners were also losing influence, as founders aged and ownership tilted toward outsiders. So a new group of professional CEOs, bred in new management schools, took the reins of corporate America.

Their grip loosened in the 1950s, when an economic boom drove a wave of investors into stocks. Increased individual ownership heightened expectations and fed a belief in shareholder democracy. New regulations requiring the disclosure of senior-management pay, along with the rise of the corporate raider, spurred a growing number of contested elections for boards, known as proxy contests. After a concerted lobbying and publicity effort on governance issues by the Business Roundtable, new regulations in 1956 clamped down on proxy battles, and CEOs prevailed at the end of the decade.

Today institutional investment is again booming. After declining to as low as 15% in the 1940s, institutional ownership returned to turn-of-the-century levels of 50% and higher in the mid-1980s. Takeovers flourished in the '80s environment of few regulatory restrictions and easy financing via junk bonds. But public opinion turned against raiders, state regulations and court decisions made takeovers more difficult, junk bonds dried up, and management created innovative takeover defenses. Many CEOs believed they had won the governance battle.

CEOs who resist pressure for strong governance risk having Calpers or regulatory bureaucrats tell them what kind of board they should have.

But institutional investors looked for other ways to prod CEOs. In 1992 the Securities and Exchange Commission made it easier for investors to coordinate on governance issues. Shareholders issued "hit lists" of underperforming companies, announced shareholder proposals and communicated directly with management. But it didn't make sense for Calpers and other institutions to intervene in each of the thousands of companies whose

stock they held. They have turned to boards—shareholders' elected representatives—as management watchdogs.

What do these investors want? The bottom line is long-term returns. The most active investors are pension funds with mind-boggling obligations. Calpers will need to be able to pay out $30 billion each year to its beneficiaries by 2020. Institutional investors rely on strong, independent boards to create shareholder value. They believe strong boards will help companies correct mistakes, recover from crises, and find, support and reward outstanding CEOs.

Numerous recent examples, along with academic research, support the notion that boards can have a significant impact on stock prices. Recent research by McKinsey in conjunction with Institutional Investor found that many large private money managers—especially those looking for long term value—are willing to pay a higher stock price for companies with good, independent board governance. We surveyed 50 money managers representing about $850 billion in assets, and found that they were willing to pay an 11% good-governance premium on average.

How should CEOs respond to the demand for strong, independent boards? Well-performing companies have the option of doing nothing for now—but only until there is a period of poor results, a complex acquisition, or a crisis. CEOs could search for ways to thwart investors, as they did in the 1980s. But underlying forces make this strategy unpromising. Institutional ownership will probably continue to increase. Public opinion is suspicious of CEOs, whose pay has dramatically increased while companies downsized. The most prominent investors, meanwhile, are more sympathetic—not the "greedy raiders" of the '80s, but institutions like Calpers, which pays the pensions of firemen, police officers and school librarians. Politicians aren't likely to attack these investors on behalf of CEOs.

Finally, the SEC has been embracing a pro-shareholder stance that seems unlikely to change.

CEOs can benefit personally from strong, independent boards. As major stockholders themselves, they should pursue strategies that increase the stock price. Harmonious relations with investors enable CEOs to focus their time and energy on substantive business issues. CEOs will find, too, that investors are much more patient and understanding in bad times if they trust the board. And while a weak board may rubber-stamp the CEO's decisions when times are good, often its first response to a crisis is to fire the CEO—whereas a strong board with substantive knowledge of strategy and company performance will tend to support management.

CEOs who resist pressure for strong governance risk having Calpers or regulatory bureaucrats tell them what kind of board they should have—an outcome that serves no one's interest. After all, the best boards aren't built by outsiders. Only the CEO has the knowledge and the position to build the optimal board for his company. Rather than fight the tides, CEOs should take the lead by tailoring strong boards for their companies, and thereby shape the next era of corporate governance to their—and their shareholders'—benefit.

Ms. van Heeckeren is a consultant in McKinsey & Co.'s Cleveland Office. Robert Felton, a McKinsey partner, contributed to this article.

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

[Caption Omitted in Printing]

DECLARATION OF JOHN C. COFFEE, JR.

JOHN C. COFFEE, JR., declares as follows:

1. I make this declaration to supplement my earlier affidavit dated June 25, 1997, and earlier filed in this proceeding. I do so in response to the letter, dated June 30, 1997, from James E. Burton, Chief Executive Officer of California Public Employees' Retirement System ("CALPERS") to G. Allen Andreas, Jr. Chief Executive Officer and President of Archer Daniels Midland ("ADM").

2. In that letter, Mr. Burton voices several criticisms of the settlement, including, most notably, the criticism that the definition of "outside" and "nonmanagement" directors in the proposed settlement is "inadequate", because it is subject to an undefined materiality standard. In this affidavit, I address only his criticism of the "materiality" exception.

3. As an abstract matter, I believe Mr. Burton is correct; that is, a definition that disqualified a director from being an independent "outside" director if such director, directly or indirectly, had any business or financial relationship with the company would be superior. A materiality standard can raise difficult interpretive issues (although precisely for this reason it may be difficult for a ADM to rely on such a materiality standard with any confidence). At the same time, however, I also recognize that

there are problems with the elimination of a materiality standard. For example, sometimes there are unknown *de minimis* relationships (such as where a law firm handles a minor matter for a subsidiary of the parent corporation on whose board one of its partners sits—without anyone recognizing the parent/subsidiary relationship). If a director were deemed not to be "independent" because of such a *de minimis* and unknown relationship, the definition of independence would sweep overbroadly.

4. While I would personally prefer the Council of Institutional Investors' definition, I do not believe that it reflects the prevailing approach today among large public corporations. Indeed, many public corporations with model corporate governance standards have not adopted this standard.

5. In that light, I understand and sympathize with Mr. Burton's criticism, but it does not cause me to alter my original judgment that ADM's new corporate governance provisions reflect the "state of the art" today.

6. I declare under the penalty of perjury that the foregoing is true and correct and that this Declaration is executed this 3rd day of July, 1997.

/s/ John C. Coffee, Jr.
JOHN C. COFFEE, JR.

Dated: July 3, 1997

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

[Caption Omitted in Printing]

DECLARATION OF ROBERT M. ROSEMAN IN OPPOSITION TO OBJECTORS' MOTION TO POSTPONE THE SETTLEMENT HEARING

I, Robert M. Roseman declare as follows:

1. I am a partner in the firm Spector & Roseman, P.C. and am counsel for plaintiffs in this action. I submit this declaration in response to California Public Employees' Retirement System ("CalPERS") and Florida State Board of Administration's ("FSBA") hereinafter referred to as the "Objectors") request that this Court postpone the hearing because the Objectors did not receive adequate notice of the Settlement.

2. Beginning in December 1996, my co-counsel, Terry Rose Saunders, and I contacted and met with a number of Archer Daniels Midland Company's ("ADM") institutional investors to solicit their view on and keep them appraised of the terms of a proposed settlement with ADM. Initially, based on comments made by Sarah Teslik, Chairperson of the Council of Institutional Investors ("CII"), I asked my associate, Jacob A. Goldberg, to contact Ms. Teslik to solicit her views.

3. When Mr. Goldberg attempted to speak with Ms. Teslik at the CII, he spoke with Ann Yerger who told Mr. Goldberg that there was no need to speak with Ms. Teslik. Ms. Yerger told Mr. Goldberg to draft and send

a letter to her describing the case and enclosing a copy of the Complaint.

4. In mid-December, Mr. Goldberg wrote to Ms. Yerger to inform her of the nature and status of the action, to send her a copy of the Complaint and to set up a meeting with her. Ms. Yerger then arranged for a meeting among Mr. Goldberg and me with Anne Hanson, a staff-person at the CII.

5. Mr. Goldberg and I had a telephone conversation with Ms. Hanson on December 19, 1996. Ms. Hansen informed us that the CII rarely involved itself in a legal action. She said that such actions were politically sensitive and that members of CII did not always agree on outcomes and solutions or with shareholder activism in general. Ms. Hanson told us that we should speak to CII's members on an individual basis. Ms. Hanson gave us the names of several CII members to contact who she believed would agree to meet with us concerning the corporate governance at ADM.

6. Additionally, during that meeting, we agreed to draft a synopsis of the derivative claims and discuss the then pending motion to dismiss for CII's "Membership Alert" news letter which Mr. Goldberg did.

7. At no time in our conversation with Ms. Hanson did she request that we keep her or CII informed of our settlement discussions or offer us assistance beyond sending us standard membership documents, including the CII definition of independence, and providing us with the names and telephone numbers of certain of her members whom she believed would be willing to meet with us.

8. Shortly after the conversation with Ms. Hanson, I met with Ed Durkin of the Carpenters' Union Pension Fund, one of ADM's largest shareholders and a member of CII. This fund had been one of the groups responsible for sponsoring a resolution concerning independence

of ADM Directors for shareholder approval at ADM's 1996 annual shareholder meeting. During this meeting, I told Mr. Durkin that it was our intent in negotiating any settlement with ADM to take into consideration ADM's institutional investors' concerns with regard to, among other things, the definition of an independent director and the need for confidential voting. I also told Mr. Durkin that we intended to meet with as many of ADM's largest shareholders to solicit their views and to let them know what we believe we can achieve in a negotiated settlement. Mr. Durkin expressed his views and provided us with names of individuals at other investor funds to contact. I also told Mr. Durkin that we would remain in contact with him and if at any time he wanted to speak with us we would be available.

9. On February 6. 1997, my co-counsel Terry Rose Saunders and I met with Kayla Gillan, general counsel of objector CalPERS, in San Francisco. We explained to Ms. Gillan the status of the litigation and settlement discussions and, in particular, discussions we had had with ADM regarding the definition of "independence", for ADM's Board of Directors. We spent approximately one and one half hours with Ms. Gillan primarily discussing our settlement negotiations with ADM.

10. We specifically advised Ms. Gillan that ADM was unwilling to adopt all of the provisions of the CII definition of independence. Ms. Gillan responded that she understood that and that a somewhat weaker definition of board-member "independence" than that of CII was "okay" because CII's definition was intended to establish a starting point for negotiations.

11. We told Ms. Gillan we could not say if and when we would conclude settlement negotiations with ADM. Ms. Gillan advised us that CalPERS might resubmit the proposal it had made in 1996 concerning the definition

of independence. We responded that we had no problem with CalPERS proceeding with a proxy proposal.

12. Ms. Gillan said that she would report our conversation to FSBA. She suggested that we meet with John Lukomnick of the New York City Pension Fund and Bart Naylor of the Teamsters Pension Fund, which we did. She commended us for taking the time to inform the institutional investors of our settlement discussions. Ms. Gillan also told us that she would forward to us names of other institutional investors with whom we might wish to meet concerning the settlement discussions. We never heard from Ms. Gillan or anyone else from CalPERS until June 30, 1997, when I received a copy of a letter to Allen Andreas from Mr. Burton of CalPERS. In fact, the week after this Court preliminarily approved the settlement, I contacted Ms. Gillan to discuss the settlement with her and to answer any questions she may have. I left a detailed message on her voice mail when informed that she was not available. She never called me back despite my attempting to contact her several times thereafter.

13. Following the preliminary approval I called each of the individuals with whom we met during the litigation to discuss the terms of the Settlement. I spoke to Bart Naylor of the Teamsters and Ed Durkin on a number of occasions.

14. Shortly after this Court's preliminary approval of the Settlement, Ms. Yerger requested a description of the current Board of ADM and who among that list ADM considered to be independent. Ms. Yerger was aware of the terms of the Settlement and questioned me about it. This conversation took place more than *one month ago*. Ms. Yerger asked me to explain the reason why ADM did not accept the CII definition. I tried to explain to her that ADM considered CII's restrictive definition to be inconsistent with the Board's right to exercise its judg-

ment in determining whether a professional, business or consulting relationship was sufficient to cause a director not to be independent. By way of example I told her that certain directors would not be independent under CII's definition because their company received monies from ADM which admittedly were not material to their company. I next spoke to Ann Yerger on June 27, 1997 when she requested copies of the papers we had filed with the Court in May 1997 in support of preliminary approval of the Settlement. I also sent her copies of the affidavits of John C. Coffee, Jr and R. Alan Miller, plaintiffs' experts.

I declare under penalty of perjury that the foregoing is true and correct and that this declaration is executed this 3rd

/s/ Robert M. Roseman
ROBERT M. ROSEMAN

Dated: July 6, 1997

IN THE UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

[Caption Omitted in Printing]

REPORT OF PROCEEDINGS

July 7th, 1997
Fairness Hearing
Before: HAROLD A. BAKER, Judge Presiding

* * * *

[2] THE CLERK: Paul Felzen et al. v. Dwayne O. Andreas, et al., 95-2279.

THE COURT: State your appearance for the plaintiffs.

MR. PHEBUS: Joseph Phebus.

MS. SAUNDERS: Good morning, Your Honor. Terry Rose Saunders.

MR. ROSEMAN: Good morning, Your Honor. Robert Roseman.

MR. HARWOOD: Good morning, Your Honor. Robert Harwood for the Delaware plaintiffs.

MR. BERNSTEIN: Good morning, Your Honor. Stanley Bernstein, for the Delaware plaintiffs.

MS. SALVETTI: Good morning, Your Honor. Susan Salvetti, for the Delaware plaintiffs.

THE COURT: For ADM.

MR. SHAFTER: Good morning, Your Honor, Jim Shafter.

MR. PECKERT: Jim Peckert.

THE COURT: Now, there are a number of objectors.

MR. MOSS: Your Honor, if I could state for the record, I am Thom Moss for the individual defendants.

THE COURT: Did I miss anybody else among the plaintiffs/defendants?

MR. DOCKTERMAN: Your Honor, I am Michael [3] Dockterman. I represent one of the additional defendants as an additional appearance filed this morning on behalf of Mr. Webb.

THE COURT: And I am sorry, Mr. Moss. I couldn't see you. All right. Now the objectors. Why don't you come up and sit in the jury box where you will be close and have a ring-side seat so to speak.

THE COURT: Very well. Mr. Dessen, how are you this morning.

MR. DESSON: Very good, sir.

MR. HANSEN: Good morning, I am Mark Hansen representing the Florida State Board of Administration.

MR. BEENCK: Good morning, Your Honor, I am Tom Beenck, I am the assistant general counsel for the Florida State Board.

MR. GLOTZER: I will introduce myself. Good morning. My name is Michael Glotzer, shareholder activist. I lay claim to being the voice of over 25 percent of the shareholders of this company limited to the subject of cumulative voting. 25 percent voted for our proposal at last year's annual meeting, so I lay claim being the spokesman. If they voted for my proposal, they certainly authorized me to speak on their behalf.

THE COURT: I saw that assertion in the materials. Again, do you want to state your appearance [4] for the record.

MR. HANSEN: Thank you, Your Honor. Good morning. My name is Mark Hansen from the Kellogg, Huber, Hansen, Todd & Evans, from Washington, and I represent here today the Florida State Board of Administration as an objector as to this proposed settlement, and the California Public Employees' Retirement System as an objector; and with me is Tom Beenck, the general counsel of the Florida State Board of Administration.

THE COURT: I don't know if you are all admitted to practice, but I will admit you *pro hac vice*.

MR. HANSEN: Thank you, Your Honor.

THE COURT: Now, do you have an interest? The people in the audience.

MS. SAUNDERS: Well, Your Honor, Mr. Miller is attending today. Mr. Miller submitted an affidavit.

THE COURT: I read his submissions, yes.

MS. SAUNDERS: He is here this morning, Your Honor, in the event that Your Honor has any questions or needs any testimony.

THE COURT: Thank you. All right. Now, the first question I gather—where is the docket sheet, Marilyn? Here I have got it. Thanks.

Is that there is a motion, I gather, by the objectors to postpone or vacate this hearing and set it for [5] another day. I will hear argument.

MR. HANSEN: Thank you, Your Honor. Shall I address the court from here?

THE COURT: Yes, you may.

MR. HANSEN: Your Honor, I represent, as I mentioned earlier, the California Public Employees' Retirement System and the Florida State Board Administration, CALPERS, as the acronym goes, has 2.7 million of ADM shares, Florida SBA has 1.7 million shares.

Your Honor, this hearing was set on May 30th upon request of the plaintiffs' counsel. It's now just—we're a month later. Through various machinations, my clients didn't really become aware of the paper regarding the settlement until about two weeks ago; and, as a result, Your Honor, given the fact that this settlement we believe is really beyond the bounds of proper settlement, we would like to raise a very strong objection to it, but, we believe, we have been hampered by the speed of which this hearing has been convened.

We have submitted an objection. We are prepared to object here today, but, we believe, Your Honor, you would have far more objectors if the hearing were postponed at least a month and we would be able to come in with more testimony to rebut the rather scarce testi

mony that is here in support of the settlement, that being Mr. Miller's [6] declarations and Mr. Coffee's declaration.

We think, Your Honor, that given the promptness of this case, given the—what we consider to be the improper terms of the settlement, we think there is no prejudice to anybody in delaying this a month so that all shareholders can be heard so we can make full and reasonable representation to the court, including testimony and other witnesses we think would support our position.

THE COURT: All right. Anybody else want to be heard in support of the motion? All right. In opposition, if you wish, you can address the court from your chair.

MS. SAUNDERS: Perhaps to save time, Your Honor, I can stand here. Terry Rose Saunders on behalf of the plaintiffs. Your Honor, we submitted this morning a declaration from Mr. Roseman which I have set—

THE COURT: I have read it.

MS. SAUNDERS: Fine.

THE COURT: I also read Professor Coffee's statement.

MS. SAUNDERS: Fine. Professor Coffee's statement goes to the merits. Mr. Roseman really goes to this motion. Your Honor, there is no reason to postpone this hearing. The investors in this company, the shareholders received notice shortly after May 30th. The [7] objector has not submitted any real evidence that they did not receive notice. In fact, the one declaration that they have submitted of Miss Yerger states that she received the settlement papers on June 3rd. That is more than a month ago.

Since this settlement was approved, we have been in touch with many institutional investors and representatives all of them are aware of this settlement.

As Your Honor knows, the problem you are aware there was great press coverage of the court's order on May 30th of the preliminary approval, and there is just

no reason that anyone could not have been properly prepared to appear this morning for this hearing.

In addition, while CalPERS and the Florida State Board are large institutional shareholders, they represent less than one percent of the shareholders or the shares of ADM. ADM has over 530 million shares outstanding. They are the only ones to come in this morning to, and seek to delay this hearing; and, again, I emphasize we have talked to other large institutional shareholders who were perfectly aware of this.

I would point out, Your Honor, it's in Mr. Roseman's declaration that he did attempt to contact CalPERS through Miss Gillan, (phonetic) who is their general counsel. Left a detailed message and she never [&] returned the call.

In addition to that, CalPERS and the Council of Institutional Investors who seems to be supporting this motion have been aware of the settlement discussions since last December. We had a meeting with Miss Gillan. I attended that meeting in February. The specific point about which they are objecting this morning was discussed at that meeting and we never heard from them again.

This case has been—we have been trying to get this settlement approved. We would like—we have Your Honor's attention this morning. Everybody is prepared. Everybody is here. And the hearing should go forward. There will be no prejudice to the objectors. There will be prejudice to the shareholders of ADM if the hearing does not go forward.

THE COURT: Anyone else want to speak? On behalf of the Delaware.

MR. HARWOOD: Thank you, Your Honor. I will try not to repeat any of Miss Saunders' argument. I would note I think there was a rather long article on the settlement which appeared in the June 2nd edition. I believe it was June 2nd edition of the Wall Street Journal and explained some of the terms, so CalPERS and

the other institutional investors were arguably on notice of that, at least since June 2nd and from the affidavits that have been submitted [9] the Institutional Investors knew that a settlement was in the works well before that.

I would also note that Institutional Investors and specifically CalPERS knows how to come in and make itself known when it wants to. It has done it in a litigation pending in the Supreme Court of New York County *In Re: W.R. Grace* where CalPERS saw fit to bring on an order to show cause to make itself either sole or an additional co-lead counsel. They know how to do it when they want to, judge.

And, fiinally, I don't know what machinations Mr. Hansen was referring to, but I know from my involvement that everything about the hearing was excruciatingly above board, and if that machinations were directed at either counsel or plaintiffs or the defendants or, indeed, the court, I think Mr. Hansen should explain himself.

MR. HANSEN: I make no assertion of any impropriety, Your Honor, but I do say coming in here after doing nothing in the case for years and having a 30-day window with this kind of what we consider outrageous settlement is far too short, judge. Far too short.

THE COURT: Why do you say they have done nothing?

MR. HANSEN: The case hasn't been litigated to a motion to dismiss. The case hasn't had real discovery. There hasn't been a single deposition taken. I have [10] studied the materials they have submitted. Again, I haven't seen the affidavit that has the backup for the fee petition.

I have seen Miss Saunders' cover affidavit, but, Your Honor, all I can see evidence of in terms of the prosecution of this case is the filing of the complaint, a dismissal without prejudice, a refiling of the complaint, dis-

covery granted only to the extent of some release of some documents that have been provided to the government.

Request for discovery stonewalled. Motion to compel, adjourned seven times. Settlement? After a period of more than a year.

And then suddenly we have thirty days to have this extraordinary settlement crammed down on the shareholders. The only shareholders we have here before the court, Your Honor, are sitting here in this box, and we don't think that's an appropriate length of time for this process to take place.

There is no reason why this had to be thirty days. I think frankly, Your Honor, that it was done in an expedited way to try and get this settlement through and to eliminate the ability of CalPERs, SBA, and the individual shareholders are here to make their full presentation to the court, and I can't see any reason, and I haven't heard it in their presentation, why this couldn't be a more [11] reasonable period.

I would note at the annual meeting of this company almost half of the shareholders, over board opposition, loaded in favor of the proposal submitted by some of the international shareholders.

There is a lot of feeling out there among the shareholders of this company about these issues, and we think, Your Honor, if there were more time this court would have a fuller record.

Your Honor, under the cases that we have cited to the court a full record is what this process is about. Objectors should be permitted a full opportunity to make a record to the court so that the court can appropriately assess its fiduciary role, which you have here, Your Honor, because you have to determine this settlement is fair to the shareholders.

Plaintiffs' lawyers have their interest, the company has its interest, the individual directors have their interest, but, Your Honor, as their own expert Mr. Coffee pointed out, derivative actions has a unique potential for collu-

sion for settlements not in the best interest of the shareholders. We think that is what has happened here.

We see no reason why, we haven't heard any reason why a reasonable period couldn't be provided so this court [12] can have a full record.

Your Honor, I have been retained no more than about ten days. I need more time to present that full record to the court. I believe that the court should adjourn this hearing. We'll have a very full record and there may be many shareholders filling this box. It's just too short a time to have a full presentation.

THE COURT: Is Miss Saunders right that your client's general counsel has been in conference, consultation, contact with the plaintiffs during the negotiated, the extensive settlement negotiations that have been going on in the case?

MR. HANSEN: Your Honor, that's precisely our point that we would love to give a full record on. We have, indeed been, in contact in dealing with plaintiffs' lawyers what a fair settlement could look like and an out product of that there were concerns that were not addressed that the settlement was, in our judgment, completely different from what we said in a decent settlement, and, in fact, the settlement is nothing more than a (unintelligible) of principles. I hate to get into the merits.

THE COURT: They didn't agree with you in summary.

MR. HANSEN: I am sorry.

[13] THE COURT: I say they didn't agree with you.

MR. HANSEN: They didn't negotiate.

THE COURT: With your clients, they didn't agree with your clients.

MR. HANSEN: They didn't pick up a phone and make phone calls. Our product wasn't productive from our standpoint, and also I think it's important to note that one of the crime (unintelligible) what they are having the court approve is that somehow they have gained the

confidence and the assent of the large institutional shareholders, if that is something that we're supporting the settlement. In fact, it's quite the contrary.

When the institutional shareholders learned what had been done, particularly, when the institutional shareholders learned what the settlement really was going to involve, that is nothing, a large payment to the lawyers and only purely cosmetic alterations of principles of the governance that has already been agreed to, Your Honor, already been agreed to by the ADM Board, the shareholders, I believe would be outraged would not be too strong a word. CalPERS and SBA has rushed here to the court to make that position known to the court.

We believe others will follow, but the time is very short. To say that because they picked up the phone we are somehow parties to the settlement, I think is [14] exactly the opposite of the truth, Your Honor. They did pick up the phone. All the more reason why they should not have entered into this what we considered an illusive settlement that benefits the lawyers and not benefit the company or its shareholders at all. So we don't believe, Your Honor, in fact, that there was conversation.

THE COURT: I thought you weren't accusing them of wrongdoing. I heard the word collusive and I have heard quite a few pejorative words.

MR. HANSEN: They are indeed pejorative. Wrongdoing. That's in the eye of the beholder. The plaintiffs have an interest here. They have a large fee petition before the court. Certainly the individual defendants have an interest here.

Frankly, I have no quarrel with the plaintiffs' lawyer getting a fair fee, and I have no quarrel with defense lawyers trying to get their clients released. Who is here for the shareholders, Your Honor? The only people here for the shareholders, and the only people who have an interest that be protected are the Institutional Investors shareholders before the court and the individual shareholders in this box.

We feel railroaded, Your Honor. We feel the shareholders—does not serve the shareholders interest, and we believe a fair presentation would prove that to the [15] court. I am not here to sling mud, Your Honor.

I do believe a settlement of a claim of $190 million worth of wrongdoing admitted by Archer Daniels Midland that legally represents only payment for lawyers, and that's in two parts, and these lawyers and an independent director committee of lawyers, and then the beauty of the settlement, Your Honor, the governance approved this.

Your Honor, I do believe that something slightly suspect in the presentation of the court about this supposed jewel talking about governance improvements, the majority of which, all of which were approved in January of 1997 by the board. Your Honor, there is something wrong with this process.

THE COURT: Coffee and Miller don't agree with you.

MR. HANSEN: Coffee and Miller do agree with you. I will speak for Coffee. Let me take Coffee's affidavit and hand it up to the court this morning. I think that's a good point. Coffee says the standards—

(Interrupted by the court reporter.)

THE COURT: You must go to a court where if he doesn't speak rapidly, he won't be heard and the trap door will open and you will disappear. Slow down.

MR. HANSEN: Your Honor, I apologize. The Second [16] Circuit did tell me about a trap door. That does explain some of my speed. Mr. Coffee, Your Honor.

THE COURT: I know what you mean. He says that he agrees that it will just be heaven if you could have the kind of governance you talk about, but he says it doesn't meet reality and that most corporations reject flatly that approach.

I think I have heard enough rebuttal unless you have some jewel you want to depart. The bobbing up and down of the other lawyers in the case, they are dying to say something, too. Mr. Shafter.

MR. SHAFTER: Your Honor, may it please the court. Counsel has given an eloquent argument on the merits of his objection. Your Honor, I do sympathize with counsel when counsel is retained late in the game. That has happened to all of us as attorneys.

But the fact that the clients knew about the settlement as set forth in Mr. Roseman's declaration it's just absolutely the case. They did know. They are here today objecting because they thing they could have done better.

Your Honor, Miss Saunders misspoke to the court when, or misstated to the court when she said that these two institutions represented one percent of the shares of ADM. All of the objectors that have filed with the court [17] whether they are proper objections or not, all of them that are on file are less than one percent.

Ninety percent have not spoken in any way. But, as the court well knows, as in most cases, what that probably indicates. Also when counsel tells you that he represents two of the more important Institutional Investors, we absolutely agree with that. ADM is proud to have SBA and CalPERS as institutional shareholders.

But, judge, as Florida and CalPERS knows we have 365 other Institutional Investors all of whom are substantial. The company doesn't even follow those institutions unless they have lots of stock in excess of 75 to 100,000 shares.

So the fact that less than one percent is here today objecting and only two of the 367 Institutional Investors that we have here objecting is important.

Now for the reason to go forward is that, as the court is aware, ADM has a quarterly board meeting on July the 17th at which time, if this settlement is approved, the board will implement those changes not mandated but ordered by this court.

There are also changes in the therapeutics that require the board to take certain action at the shareholders meeting in October, and the changes that we are going to make are not changes in principle, they are [18] going

to be ordered by this court and we are changing our bylaws and our annual meeting is in October. And we have to tell our shareholders about those things.

We have to get the proxies out and that was the date this hearing was selected. Mr. Hansen is probably not aware that primarily practicing in Washington, D.C., but Mr. Phebus, Mr. Moss, and I know that the court does not sit regularly here in Urbana during the summer months and the court specifically set this hearing today while the court was here.

Judge, it is very important that this go forward. As the court has on file today our affidavit of mailing. There has been in excess of 200,000 first class notices sent out. People got notices. If they wanted to object, they are here. These are very sophisticated investors and they have obviously excellent legal representation here today.

The court should summarily deny the request for a continuance if for no other reason simply because you don't address a federal court by letter. You do it in a motion. The Seventh Circuit has spoken on that a number of times. This court has spoken on that a number of times. I would ask the court to call the matter for hearing on the merits.

THE COURT: Anybody else on behalf of the plaintiffs? I will come back to you. You will be heard [19] in full.

MR. ROSEMAN: Robert Roseman, Your Honor, as the point person for plaintiffs, my name is on the notice and I did receive a substantial amount of phone calls from shareholders, in excess of fifty, and by and large they were asking questions about do I submit a claim form, thinking that this was a class action.

But from those fifty shareholders I did not receive any indication that they were going to object. In fact, we were complimented on the settlement. I did speak, in addition to trying to speak to CalPERS, I did speak to the CalPERS Pension Fund. The Teamsters spoke to people whom we met with early on and they were basically

pleased with the settlement, although they would like to see things differently.

Of the information we received how can you object to something which is positive? And having met with those institutions and having spoken with them after the settlement was approved, they certainly had the opportunity to object and they chose not to.

THE COURT: Thank you, counsel.

MR. GLOTZER: My name is Martin Glotzer of Chicago. I believe, judge, you acknowledged the fact that I made the statement that I am a spokesman for shareholders only twenty-five percent of the company shares limited to [20] cumulative voting, and I would like that part of the record. The lawyers for the plaintiffs say there was only a few shareholders. Twenty-five percent of the shareholders are represented by me. I am their voice.

THE COURT: I recognize that that is your assertion. I saw that in the materials that I looked through in the past three days. That is your assertion. I didn't say I agreed with you.

* * * *

[79] THE COURT: All right. The court's ready to rule. Having heard the remarks of the proponents of the settlement and the remarks of those in opposition, the court concludes that the settlement, which is before the court is fair, reasonable, and adequate. The court considers the strength of the plaintiffs' claims in the case as balanced against what was obtained in the settlement.

[80] The case the plaintiffs had was not, as one of my colleagues described, "another case as a dead bang winner." Far from it. There were serious questions raised in the motion to dismiss, and I tried to look back through the record to see what discovery wasn't afforded and I think that pool of documents was available, and I can remember discussions with counsel in this case and in the other civil ADM cases that were pending about the availability of the document pool that had been created by

Judges, Shadur, Mihm, and I don't know about the judge in California participating in that, but I believe all of that information was available to the plaintiffs in the case.

So that the record really is slightly misleading as far as discovery is concerned because the plaintiffs did have all of that information available to them.

In addition, the parties, as you see from the docket, got to the point where they were squabbling about compelling discovery and having a hearing on the motion to dismiss, and the defendants kept asking to advance the hearing on the motion to dismiss, and then they began negotiaitons in the case and the court abstained from hearing or ruling on the motion at the request of the parties so that they could talk to each other.

Well, because lawyers talk to each other doesn't mean that the lawyers are in collusion. Far from it. Of [81] course, quite obviously they have to communicate and talk if they are going to find some alternative means of settling their disputes other than going to judgment in a court of law.

The defendants' ability to pay. There is a ten million dollar cap on the insurance. Mr. Hansen suggests that the directors had deep pockets. I have been in the legal profession and the litigation end of it for over forty years, I am sorry to say, and I wonder if he has ever tried to pursue a suit for transferring assets in fraud of creditors. That needs a good deal of luck.

And to assume that those directors are holding all of their assets, I think is an unwarranted assumption, so that the ten million dollars is a realistic sum to think was available; at least it was readily available—obviously available.

The complexity, length, and expense of further litigation also has to be considered. This case would have gone on for years. I wouldn't have had to suffer through it, being a senior judge somebody else could have taken it over, but my guess would be five years of further litigation.

The amount of opposition to the settlement. That's been commented upon by the proponents of the settlement. While the objections I am sure are heartfelt [82] and sincere, they really represent a very very small percentage of the shareholders of the corporation. The Not that the objections aren't to be discounted just because they are small—from a small number, relatively small number of shareholders, but still the overwhelming reaction to the proposed settlement has been acceptance.

I had no idea Edward Dessen was going to appear. I have known him for years. He is a businessman. He owns property. He is a very outspoken person, and, true, with faint praise, he approved the settlement. He may be reflective of the way a large percentage of shareholders feel. Well, it's a start. It's a beginning.

I find no basis for claims of collusion. Just none. These people have dealt with each other professionally and at arm's length as far as the progress of the case has been concerned.

Certainly competent counsel with experience has expressed support for the settlement. I have to respect that. And I have already spoken a little bit about the stage of the proceedings and the amount of discovery. The case has gone on for two years. A great deal—a substantial portion of which has been devoted to attempting to finding an alternative to the settlement of the dispute.

* * * *

IN THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF ILLINOIS
URBANA, ILLINOIS

Case No. 95-2279

Honorable Harold A. Baker
Judge Presiding

PAUL FELZEN, TRUSTEE OF LOUISE LASKIN TRUST—1991 and SANDRA ESNER,
Plaintiffs,

v.

DWAYNE O. ANDREAS, *et al.*,
Defendants,

and

ARCHER DANIELS MIDLAND COMPANY,
a Delaware Corporation,
Nominal Defendant.

IN THE COURT OF CHANCERY
OF THE STATE OF DELAWARE
IN AND FOR NEW CASTLE COUNTY

Consolidated C.A. No. 14403

IN RE: ARCHER DANIELS MIDLAND COMPANY

NOTICE OF APPEAL BY CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM AND FLORIDA STATE BOARD OF ADMINISTRATION

Notice is hereby given that Objectors California Public Employees' Retirement System ("CalPERS") and Florida State Board of Administration ("SBA"), each of whom is entitled to appeal from the Final Judgment and Order of Dismissal (July 7, 1997), and Order Awarding Attorneys' Fees and Reimbursement of Expenses (July 7, 1997), hereby appeal from such Judgment and Order to the United States Court of Appeals for the Seventh Circuit.

A joint appeal is practicable because, as is described in CalPERS and SBA's joint Objections to the Settlement (July 3, 1997), CalPERS and SBA's interests are aligned.

Respectfully submitted,

/s/ Mark C. Hansen
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Dated: July 14, 1997

[Filed Aug. 15, 1997]

IN THE UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

[Caption Omitted in Printing]

PLAINTIFFS' MOTION TO DISMISS THE APPEAL OF NON-PARTIES

Plaintiffs-Appellees Paul Felzen, Trustee of Louise Laskin Trust—1991 and Sandra Esner ("Plaintiffs") move this Court for an Order dismissing the joint appeal filed by California Public Employees Retirement System ("CalPERS") and Florida State Board of Administration ("SBA") for the reason that, under the established law of this Circuit as recently reaffirmed in *In re: Brand Name Prescription Drugs Antitrust Litigation*, 115 F.3d 456 (7th Cir. 1997), as amended at 1997 U.S. App. LEXIS 12628 at *3, CalPERS and SBA have no right to appeal. CalPERS and SBA are not parties to the derivative action in which the Judgment and Order they seek to appeal were entered, and neither CalPERS nor SBA sought to intervene in the district court. Plaintiffs submit their memorandum of law in further support of this motion.

WHEREFORE, plaintiffs request that the appeal be dismissed.

Respectfully submitted,

By: /s/ Terry Rose Saunders
One of the Attorneys for Plaintiffs-Appellees
Paul Felzen, Trustee of Louise Laskin Trust
—1991 and Sandra Esner

[Counsel Listing Omitted]

SUPREME COURT OF THE UNITED STATES

No. 97-1732

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM, *et al.*,
Petitioners

v.

PAUL FELZEN, *et al.*

ORDER ALLOWING CERTIORARI

Filed September 29, 1998

The petition herein for a writ of certiorari to the United States Court of Appeals for the Seventh Circuit is granted limited to Question 1 presented by the petition. The brief of the petitioner is to be filed with the Clerk and served upon opposing counsel on or before 3 p.m., Tuesday, November 10, 1998. The brief of respondents is to be filed with the Clerk and served upon opposing counsel on or before 3 p.m., Tuesday, December 8, 1998. A reply brief, if any, is to be filed with the Clerk and served upon opposing counsel on or before 3 p.m., Tuesday, December 29, 1998. Rule 29.2 does not apply. Justice O'Connor took no part in the consideration or decision of this petition.

September 29, 1998

(18)

No. 97-1732

Supreme Court, U.S.
FILED
NOV 10 1998
CLERK

IN THE
Supreme Court of the United States
OCTOBER TERM, 1998

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM and FLORIDA STATE BOARD OF ADMINISTRATION,
Petitioners,

v.

PAUL FELZEN, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

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BRIEF FOR PETITIONERS

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QUESTION PRESENTED

Whether a shareholder who, pursuant to Federal Rule of Civil Procedure 23.1, is summoned to appear in federal district court and present objections to a proposed dismissal or settlement of a derivative action must also intervene pursuant to Federal Rule of Civil Procedure 24 in order to appeal an adverse decision.

PARTIES TO THE PROCEEDINGS BELOW

The following persons or entities were parties to the proceedings in the court of appeals:

California Public Employees' Retirement System
Florida State Board of Administration
Paul Felzen
Louise Laskin Trust
Sandra Esner
Dwayne O. Andreas
Ralph Bruce
John H. Daniels
Howard G. Buffett
Lowell W. Andreas
James R. Randall
Michael D. Andreas
H.D. Hale
O. Glenn Webb
Martin Andreas
Margaretta Rockefeller
F. Ross Johnson
Ray A. Goldberg
Gaylord O. Coan
John K. Vanier
Shreve M. Archer, Jr.
M. Brian Mulroney
Robert S. Strauss
Archer Daniels Midland Company

PARENT COMPANIES AND NONWHOLLY OWNED SUBSIDIARIES

California Public Employees' Retirement System and Florida State Board of Administration are governmental pension funds that have no parent companies or subsidiaries that have issued shares to the public.

TABLE OF CONTENTS

	Page
QUESTION PRESENTED	i
PARTIES TO THE PROCEEDING BELOW	ii
PARENT COMPANIES AND NONWHOLLY OWNED SUBSIDIARIES	ii
TABLE OF AUTHORITIES	iv
OPINIONS BELOW	1
JURISDICTION	1
RULES AND STATUTE INVOLVED	2
STATEMENT OF THE CASE	2
A. Background and Prior Proceedings	2
B. The Decision Below	9
SUMMARY OF THE ARGUMENT	10
ARGUMENT	13
SHAREHOLDERS WHO APPEAR IN DISTRICT COURT PURSUANT TO RULE 23.1 TO OBJECT TO A DERIVATIVE SUIT SETTLEMENT ARE ENTITLED TO APPEAL THE COURT'S APPROVAL OF THAT SETTLEMENT	13
A. Rule 23.1, This Court's Decisions, and Long-Standing Common Law Tradition Support Objectors' Right To Appeal Settlement Approvals	16
B. None of the Seventh Circuit's Arguments Supports a Requirement That Objectors Intervene in Order To Appeal	22
C. An Intervention Requirement Would Create Significant Disincentives to Objector Participation Without Serving any Countervailing Purposes	32
CONCLUSION	40

TABLE OF AUTHORITIES

Cases — Page

Ackerman v. Kassar, No. 91-56521, 1993 U.S. App. LEXIS 22074 (9th Cir. Aug. 26, 1993) 37, 38
Ackert v. Ausman, 217 F. Supp. 934 (S.D.N.Y. 1963) 16
Angoff v. Goldfine, 270 F.2d 185 (1st Cir. 1959) 26
Attorney General v. North Am. Life Ins. Co., 77 N.Y. 297 (1879) 19
Baldwin-United Corp., In re, 770 F.2d 328 (2d Cir. 1985) 26
Bayard v. Lombard, 50 U.S. (9 How.) 530 (1850) 25
Bell Atlantic Corp. v. Bolger, 2 F.3d 1304 (3d Cir. 1993) .... *passim*
Centocor, Inc. Sec. Litig., In re, No. 92-CV1071, 1993 U.S. Dist. LEXIS 7229 (E.D. Pa. June 2, 1993) 38
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Ex parte Cockcroft, 104 U.S. 578 (1882) 25
Cohen v. Beneficial Indus. Loan Corp., 337 U.S. 541 (1949) 13, 18
Cohen v. Young, 127 F.2d 721 (6th Cir. 1942) 16, 21, 32
Commercial Sec. Bank v. Walker Bank & Trust Co., 456 F.2d 1352 (10th Cir. 1972) 26
Cramer v. General Tel. & Elecs. Corp., 582 F.2d 259 (3d Cir. 1978) 17
Cunningham v. English, 269 F.2d 539 (D.C. Cir. 1959) 31
Daily Income Fund, Inc. v. Fox, 464 U.S. 523 (1984) 15, 18
Dietrich Corp. v. King Resources Co., 596 F.2d 422 (10th Cir. 1979) 26

TABLE OF AUTHORITIES—Continued

Page

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	Page
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	Page
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	Page
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28 U.S.C. § 1291	1, 23, 28
Fed. R. App. P.:	
Rule 1	1
Rule 1(b)	12, 28
Rule 3(c)	12, 28, 29

TABLE OF AUTHORITIES—Continued

	Page
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Rule 23	1
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Rule 23.1	*passim*
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	Page
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	Page
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1998

No. 97-1732

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM and FLORIDA STATE BOARD OF ADMINISTRATION,
Petitioners,

v.

PAUL FELZEN, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

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BRIEF FOR PETITIONERS

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-10a) is reported at 134 F.3d 873. The trial court's judgment and order approving the derivative suit settlement (Pet. App. 11a-15a) and the attorneys' fee award (Pet. App. 16a-17a) are not reported.

JURISDICTION

The judgment of the court of appeals was entered on January 21, 1998. The petition for a writ of certiorari was filed on April 21, 1998, and was granted on September 29, 1998. The jurisdiction of this Court rests on 28 U.S.C. § 1254(1).

RULES AND STATUTE INVOLVED

This case involves Federal Rules of Civil Procedure 23, 23.1, and 24; Federal Rules of Appellate Procedure 1 and 3; and 28 U.S.C. § 1291. Those provisions are reproduced in the addendum attached to this brief.

STATEMENT OF THE CASE

The Federal Rules of Civil Procedure recognize the unique interest that shareholders have in the terms under which a derivative suit is settled. Unnamed shareholders in a Rule 23.1 derivative suit are notified of any pending settlement and invited to appear and present their objections in district court. It is well established that they need not intervene pursuant to Rule 24 in order to do so. By virtue of their status as shareholders, they are recognized as *de facto* parties to the derivative action, and they have an absolute right to appear and register any objections without undertaking the significant additional cost and inconvenience required by formal intervention.

The question in this case is whether such a shareholder—summoned to court pursuant to Rule 23.1, but not an intervenor under Rule 24—may appeal an adverse decision on his objections to the settlement by virtue of his recognized status as a *de facto* party. The objecting shareholder has this right as a matter of law, and the facts of this case illustrate why that rule is sensible: a right to appeal is a necessary component of Rule 23.1's right to object.

A. Background and Prior Proceedings

ADM's Price Fixing Scheme. At midnight on June 27, 1995, more than 100 FBI agents raided the corporate headquarters of Archer Daniels Midland ("ADM") and the homes of ADM's top executives. The next day, ADM issued a press release announcing that three separate federal grand juries were investigating whether the company's officers had conspired with rivals to fix prices for citric acid, high fructose corn syrup, and lysine.

The government ultimately amassed overwhelming evidence of illegal and anticompetitive activity by ADM. The FBI obtained audio tapes, video tapes, and documents establishing that ADM executives conspired with at least three Asian companies to set prices and production quotas. Top ADM executives were captured on tape telling their competitors that "the competitor is our friend, and the customer is our enemy." Three executives of the other companies pleaded guilty to the conspiracy and testified that they met several times with ADM executives to set lysine prices and market shares.

On October 15, 1996, ADM pleaded guilty to criminal antitrust charges and paid a $100 million fine, the largest criminal antitrust fine ever imposed. It cost the company another $90 million to settle three civil antitrust lawsuits filed by ADM competitors. Three ADM executives—including Michael Andreas, an ADM executive vice president and the son of Dwayne O. Andreas, ADM's chief executive officer since 1970—were subsequently convicted of price fixing.

Many of ADM's troubles, in the view of shareholders and informed observers, derived from the personal, professional, familial, and financial connections between management and the members of the company's board charged with management oversight. The *Wall Street Journal*, for instance, condemned Dwayne Andreas for "stuff[ing] his board with family and friends and company officers and pa[ying] them more than twice the norm [to serve as corporate directors]." [1] A University of Chicago Business School professor similarly decried the fact that ADM had become essentially a "private fiefdom of the Andreas folks." [2] In October 1995, the California Public Em-

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[1] Roger Lowenstein, *Corporate Governance's Sorry History*, Wall St. J., Apr. 19, 1996, at C2.

[2] Martha Irvine, *Guilty Verdict May Change Plans for Top Management at Agribusiness*, Assoc. Press, Sept. 20, 1998 (quoting Professor Sam Peltzman).

ployees' Retirement System ("CalPERS") awarded ADM a grade of "F" based on its lack of adherence to accepted corporate governance principles.[3] *Business Week* rated ADM's board the single worst in America.[4]

In response to these criticisms and the federal criminal probe, ADM commissioned a report to propose corporate governance reform measures. But the report, adopted in January 1996, did little to vouchsafe true board independence. While it nominally required for the first time that the board include a majority of independent members, even persons having obvious and substantial financial ties to ADM could qualify as "independent" under the new rules. Indeed, any director could qualify as "independent" so long as ADM did not, in its absolute discretion, consider his or her relationship with the company to be "material."

Many of ADM's major shareholders, including CalPERS and the Florida State Board of Administration ("SBA"), thought this supposed "reform" inadequate. These shareholders submitted a proposal that no one with *any* personal or financial ties to the company could serve as an "independent" director. That proposal was modeled on standards for corporate independence developed by the Council of Institutional Investors (the "Council"). *See* Exh. A (Council standards) to Declaration of Sarah A.B. Teslik (July 3, 1997) (R.83).[5] Although that independ-

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[3] Greg Burns, *A Grain of Activism at Archer Daniels Midland*, Bus. Wk., Nov. 6, 1995, at 44 (Exh. H to Declaration of Steven F. Benz ("Benz Decl.") (July 3, 1997) (R.82). For the Court's convenience, citations to record materials are identified by title and the corresponding numerical designation on the district court's docket sheet, *e.g.*, R. 82.

[4] John A. Byrne, *The Best and the Worst Boards*, Bus. Wk., Nov. 25, 1996 (Exh. B to Benz Decl. (R.82)).

[5] The Council is an association of more than 100 corporate, public, and union pension funds devoted to addressing their members' investment concerns and to promoting responsible corporate governance rules and procedures. "The first and probably the most central of the Council's policies is its requirement that a majority of a corporation's directors" be independent from *any* potentially compromising relationships to the company they serve. *Id.* ¶ 4.

ence policy has been adopted by nearly 85 percent of all S&P 500 companies (*id.* ¶ 7), it was vehemently opposed by ADM management at the 1996 annual shareholder meeting. Nevertheless, the proposal garnered 41.6 percent of the vote. *Id.* ¶ 10.

The Derivative Lawsuit. In the wake of the federal criminal probe, plaintiffs' lawyers dashed to the courthouse to file shareholder derivative actions against ADM's directors. By May 1996, the suits were consolidated in the Central District of Illinois. The consolidated suit accused ADM's directors of "gross mismanagement" by failing to supervise company employees properly. Am. Compl. ¶ 1 (May 17, 1996) (R.28). Plaintiffs specifically condemned the fact that "a majority of [ADM's directors] are interested and/or lac[k] independence" from the Andreas family (*id.* ¶ 28) and charged that Dwayne Andreas "controlled and dominated the process by which each defendant director was selected for nomination or renomination to the ADM Board" (*id.* ¶ 28(a)(1)).

Plaintiffs sought recovery of the $190 million ADM had been forced to pay in criminal fines and civil settlements. Indeed, plaintiffs' attorneys touted to the Council that "a primary goal of our litigation is to recover for ADM as much of the wasted $190 million as is reasonably and realistically possible." Objections of CalPERS and SBA to Proposed Settlement of Derivative Action (July 2, 1997), Exh. A at 2 (Dec. 15, 1996 letter) (R.81). Plaintiffs' expert opined that total damages to the company were even higher—$250 million or more. Declaration of R. Alan Miller ("Miller Decl.") ¶ 11 (June 30, 1997) (R.75).

Plaintiffs' counsel, however, did almost nothing to prosecute the case. In the over two years the case was pending, there is no record of either side issuing interrogatories, seeking or taking depositions, or propounding third-party subpoenas. Plaintiffs did file a three-page motion to compel production of certain documents. *See* Plaintiffs' Motion to Compel Discovery (July 10, 1996) (R.33). But that motion was never ruled upon and plaintiffs never pressed the issue. *Id.*

What little energy plaintiffs' lawyers expended on this case was in settlement discussions with the insurance company covering ADM and its board members. In the resulting agreement ("Settlement"), reached on May 29, 1997, plaintiffs' attorneys agreed to release "any and all causes of action" against ADM and the director defendants in return for $8 million—just 3.2 percent of the $250 million in claimed damages and less than 4.3 percent of the $190 million ADM paid in fines and compensation to the government and competitors.

Plaintiffs' attorneys, ADM, and the directors then went on to allocate that fund *exclusively* to pay attorneys' fees. Nearly half of the fund was earmarked directly for the attorneys bringing suit.[6] The other half was designated for payment of *future* legal fees to be incurred by ADM in attempting to reform itself.[7] Not one dime was

[6] The parties signed a so-called "free sailing provision" under which defendants agreed not to oppose a fee petition seeking as much as $3.92 million, or 49 percent of the fund, to plaintiffs' counsel. The average fee award in shareholder derivative suits where no monetary settlement is made (effectively the case here) is $287,000. Roberta Romano, *The Shareholder Suit: Litigation Without Foundation?*, 7 J.L. Econ. & Org. 55, 63 (1991). Even in cases where monetary settlements are made to shareholders, fee awards average no more than 24 percent of the settlement amount. *Id.*

[7] Adding to the conflict of interest, plaintiffs' attorneys remained eligible under the Settlement to earn these fees as well.

returned to the corporation for the benefit of shareholders who lost at least $190 million in value as a result of their fiduciaries' misconduct.

Plaintiffs' attorneys claimed that they had extracted corporate governance reform concessions from ADM and that such reforms represented value to shareholders in excess of $158 million. Plaintiffs' Memorandum in Support of Joint Application for Award of Attorneys' Fees and Reimbursement of Expenses at 3, 7-8 (June 30, 1997 (R.73)); Miller Decl. (R.75). In fact, however, plaintiffs' "reform" measures were valueless, simply restating measures ADM had independently adopted a year earlier. For instance, though nominally requiring a majority of "independent" directors, the Settlement, just like the ADM measures adopted a year earlier, permits a director to qualify as "independent" so long as ADM does not consider its relationship with the director to be "material." *See* Declaration of Ann L. Yerger ¶¶ 9-10 (July 3, 1997) (R.81). Plaintiffs' own counsel acknowledged that the Settlement's corporate governance principles were selected precisely because they would not require ADM to change its board *in any way*. *Id.*[8]

The day after executing the Settlement, the plaintiffs' lawyers and ADM filed an agreed written motion seeking approval from the district court. The very same day, the court heard the parties and tentatively approved their deal. In accordance with Rule 23.1's requirement that "notice of the proposed dismissal or compromise shall be given to shareholders," however, the district court ordered the parties to notify all ADM shareholders of the Settlement by mail and directed them to appear if they had any objections. Order Preliminarily Approving Settle-

[8] Even two attorneys whose law firms provide legal services to the company and two executives whose companies or their affiliates do business with ADM qualified under plaintiffs' measure as "outside" directors. *Id.*

ment and Providing for Notice at 3 (May 30, 1997) (R.62) (notice directing "[a]ny shareholder of record of ADM" to "appear and show cause, if he, she or it has any [reason] why the proposed settlement of the derivative claims . . . should or should not be entered thereon"). The court set a deadline of July 3, 1997, for any written objections and scheduled a final hearing for July 7, 1997. *Id.* at 2, 3.

Petitioners, accordingly, had less than four weeks (once they actually received the notice) to review the Settlement notice, hire counsel, obtain and review copies of pleadings in the case, weigh the fairness of the Settlement, draft a brief, and appear in court in Decatur, Illinois. Moreover, plaintiffs did not file their voluminous fee petition until June 30, 1997, leaving petitioners just four days to gain access to, review, analyze, and respond in writing to that document as well.

Petitioners timely submitted their written objections and appeared at the July 7 hearing. They asked the court to reject the Settlement on the grounds that it provided little or no benefit to the corporation: the cash benefit was all to lawyers and was excessive, and the corporate governance "concessions" provided no material benefit to shareholders beyond what ADM had itself adopted a year earlier.[9] Alternatively, petitioners asked the court to order the settling parties to show cause why the corporate governance provisions should not be revised to require adherence to independence standards adopted by 85 percent of major U.S. corporations.

At the conclusion of the hearing—at which no evidence was taken—the district court approved the Settlement.

[9] Petitioners first asked the court to delay the hearing on the ground that petitioners had not been afforded sufficient time to prepare their objections. The court denied that request.

The court also awarded plaintiffs counsel fees of $3.92 million.[10] Petitioners filed a timely notice of appeal.

B. The Decision Below

Before petitioners could be heard on the merits of their appeal, the named shareholder plaintiffs (not joined by ADM or its director defendants) moved to dismiss the appeal. Though the district court had expressly summoned petitioners to participate in this case pursuant to Rule 23.1, plaintiffs argued that CalPERS and SBA could not appeal without also intervening pursuant to Rule 24.

Seventh Circuit law at that time did not require intervention pursuant to Rule 24 as a condition for appealing. As then-Judge Stevens explained in *Tryforos v. Icarian Development Co.*, 518 F.2d 1258 (7th Cir. 1975), *cert. denied*, 423 U.S. 1091 (1976), the law was "clear that a non-party shareholder who appears, pursuant to a Rule 23.1 notice, to present objections to a proposed dismissal or settlement of a derivative action may appeal an adverse decision even though he has not been formally made a party to the action" through intervention under Rule 24. *Id.* at 1263 n.22.

A panel of the Seventh Circuit, however, used this case as a vehicle for overruling *Tryforos* and holding that Rule 24 intervention is a prerequisite to any appeal by an objecting shareholder. Pet. App. 1a-4a. The panel based

[10] Even some of the plaintiffs' attorneys conceded that the fee award was excessive. *See* Memorandum on Behalf of Delaware Plaintiffs in Support of the Proposed Settlement and Award of Fees and Expenses at 1 (June 30, 1997) (R.68) (seeking fee award totaling 33⅓ percent of common fund instead of 49 percent); Hearing Tr. at 98, 102 (July 7, 1997) (R.103) (plaintiffs' counsel arguing that "[w]e don't endorse" "award of up to 49 percent of the fund"; criticizing 49 percent fee award and stating "I think if a notice went out that said that plaintiffs' counsel will apply for what is normally almost understood to be up to a third, you would have a lot fewer objections, maybe CalPERS would have elected not even to object to the fee").

its ruling on language from this Court's intervening *per curiam* opinion in *Marino v. Ortiz*, 484 U.S. 301 (1988). There the Court refused to hear an appeal by nonclass member white police officers concerning a class action settlement between a plaintiff class of black officers and the defendant police administration. In doing so, the Court commented that it is "better practice" to require Rule 24 intervention before hearing such complete strangers to the case on appeal. *Id.* at 304. From that single statement, the court of appeals inferred that shareholders —persons who, unlike the putative appellants in *Marino*, were expressly invited to participate in trial court proceedings under Rule 23.1 and whose rights were necessarily being adjudicated in the derivative action—must always intervene under Rule 24 in order to pursue an appeal.

The Seventh Circuit frankly admitted not only that its decision required reversal of circuit precedent, but also that it was in direct conflict with decisions in other courts of appeals. Pet. App. 2a, 6a-7a. The Third Circuit has rejected the necessity of Rule 24 intervention by shareholders already admitted to the case under Rule 23.1. *Bell Atlantic Corp. v. Bolger*, 2 F.3d 1304 (3d Cir. 1993); *see also Rosenbaum v. MacAllister*, 64 F.3d 1439, 1442 (10th Cir. 1995); *Gottlieb v. Wiles*, 11 F.3d 1004, 1011 (10th Cir. 1993).

SUMMARY OF ARGUMENT

A. The rights of absent shareholders are necessarily adjudicated by any settlement of a derivative action—they are thus, by necessity, *de facto* parties to the case. In recognition of that fact, Federal Rule of Civil Procedure 23.1 mandates that no derivative suit may be settled before all shareholders are notified and given an opportunity to object.

It is undisputed that shareholders may press their objections to a settlement in district court *without* undertaking the burdens associated with intervention. The question here is whether that rule should be turned on its head when a case reaches the appellate level. It should not. The ability of a shareholder to appeal is coterminous with his ability to object in district court. Both stem from the same source—the fact that the shareholder's rights are being adjudicated in the action.

The common law has long recognized that *de facto* parties may appeal without intervening in circumstances like this one. Rule 23.1 was intended to embody, not reject, that common law practice. Indeed, just a few years before the Federal Rules were adopted, this Court expressly concluded that nonparty corporate objectors could appeal a district court's decision in the related context of a receivership. *See Johnson v. Manhattan Ry.*, 289 U.S. 479 (1933). That ruling is bolstered by many federal court decisions both before and after the adoption of the Federal Rules.

B. The Seventh Circuit could identify no constitutional or statutory reason to depart from this established practice, nor does any such reason exist. The circuit court, accordingly, relied nearly exclusively on an extremely broad—and wholly untenable—understanding of a snippet of language from this Court's *per curiam* opinion in *Marino v. Ortiz*. But *Marino* did not involve the rights of shareholders in derivative suits or even of absent class members in the analogous class action context. Rather, it dealt with the rights of strangers to the case who had not been invited to appear in district court and whose rights are nowhere recognized by the Federal Rules. Accordingly, that case does not apply here. Indeed, if the Seventh Circuit's overreading of *Marino* were correct, *no* nonparty could ever appeal, an extremely dubious result that would overrule countless cases and that even respondents do not defend.

The Seventh Circuit's understanding of Federal Rule of Appellate Procedure 3(c) is equally unpersuasive. The title of that rule makes plain that it is concerned only with the formal "content[s] of the notice of appeal," not, as the Seventh Circuit concluded, with the limits of appellate jurisdiction. Indeed, the Federal Rules of Appellate Procedure elsewhere make plain that they are not intended to limit the courts of appeals' jurisdiction. *See* Fed. R. App. P. 1(b). Finally, as with its understanding of *Marino*, the Seventh Circuit's reading of Rule 3(c) would lead to the highly unlikely result that the scores of cases authorizing nonparty appeals in a variety of circumstances were all wrongly decided and must be overruled.

C. In addition to all its other flaws, the Seventh Circuit's holding undermines the central policy behind Rule 23.1—preventing collusive settlements and providing the federal courts with the information necessary to evaluate the adequacy of any proposed agreement. It is far from clear, as a legal matter, that shareholders would be allowed to intervene in order to object to a settlement. Even if they were, however, intervention involves significant burdens—such as drafting the equivalent of a complaint, submitting to the mandatory disclosure requirements of the Federal Rules, and subjecting oneself to depositions, interrogatories, and document requests. The result would be much less participation by dissenting shareholders at both the trial and appellate levels, and more approvals of inadequate and collusive derivative suit settlements—exactly what Rule 23.1 is intended to prevent.

That unfortunate consequence would not be offset by *any* countervailing benefit. Neither the Seventh Circuit nor respondents have identified a legitimate goal that their proffered rule would advance. There is simply no reason to require objecting shareholders—who appear in response to a specific invitation from the Court to show cause why they should not be bound by a settlement—to obtain an additional stamp on their passport before proceeding to the court of appeals.

ARGUMENT

SHAREHOLDERS WHO APPEAR IN DISTRICT COURT PURSUANT TO RULE 23.1 TO OBJECT TO A DERIVATIVE SUIT SETTLEMENT ARE ENTITLED TO APPEAL THE COURT'S APPROVAL OF THAT SETTLEMENT.

The shareholder derivative suit is the "chief regulator of corporate management" in American law. *Cohen v. Beneficial Indus. Loan Corp.*, 337 U.S. 541, 548 (1949). It "protect[s] the interests of the corporation from the misfeasance and malfeasance of faithless directors and managers." *Kamen v. Kemper Fin. Servs., Inc.*, 500 U.S. 90, 95 (1991) (internal quotation marks omitted). Derivative suits, accordingly, are designed to serve the twin goals of compensating the injured corporation and shareholders for managerial wrongdoing and deterring such misconduct in the first instance.[11]

Derivative suits, however, "are uniquely vulnerable to collusive settlements that benefit plaintiffs' attorneys rather than their clients." John C. Coffee, Jr., *Understanding the Plaintiff's Attorney: The Implications of Economic Theory for Private Enforcement of Law Through Class and Derivative Actions*, 86 Colum. L. Rev. 669, 677 (1986). As Judge Posner has explained, plaintiffs' counsel have a strong economic incentive "to offer to settle with the defendant for a small judgment and a large legal fee." Richard A. Posner, *Economic*

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[11] *See* Susanna M. Kim, *Conflicting Ideologies of Group Litigation: Who May Challenge Settlements in Class Actions and Derivative Suits?*, 66 Tenn. L. Rev. ——, —— (publication expected Dec. 1998); John C. Coffee, Jr. & Donald E. Schwartz, *The Survival of the Derivative Suit: An Evaluation and a Proposal for Reform*, 81 Colum. L. Rev. 261, 302-08 (1981).

Analysis of Law § 21.9, at 570 (4th ed. 1992). On the other side of the table, "such an offer will be attractive to the defendant, provided the sum of the two figures is less than the defendant's net expected loss from going to trial." *Id.* And the shareholder who nominally brought the suit generally has insufficient incentive to police such a settlement. *Id.* This case—where the Settlement represented less than 4 percent of the damage done to the company and *all* of that money was earmarked for attorneys' fees (*see supra* page 6)—is a paradigmatic example of the problem.

Federal Rule of Civil Procedure 23.1 is the judicial and legislative response to this inherent and widely recognized difficulty in derivative litigation. Rule 23.1—which like all the Federal Rules is promulgated by this Court and reviewed by Congress—provides that, before a district court approves any derivative suit settlement, "notice of the proposed . . . compromise shall be given to shareholders."

The Federal Rules thus guarantee all shareholders notice and an opportunity to participate in settlement review proceedings. The rules do so in recognition of the fact that, although a derivative suit may be brought in the name of a single shareholder, absent shareholders are *de facto* parties whose derivative rights will be resolved in the suit as well. *See, e.g., Wolf v. Barkes*, 348 F.2d 994, 996 & n.2 (2d Cir.) (Friendly, J.) (Rule 23.1's "objective" was to ensure that absent shareholders receive notice and may participate before their rights are adjudicated), *cert. denied*, 382 U.S. 941 (1965).

These absent shareholders also play a critical role in ensuring the fairness of any settlement and deterring collusion and abuse. As Professors Wright, Miller, and Kane have explained, Rule 23.1's invitation for objectors to make their views heard in district court "is intended to discourage the private settlement of a derivative claim under which a shareholder-plaintiff and his attorney personally profit to the exclusion of the corporation and the other shareholders." 7C Charles A. Wright, Arthur R. Miller & Mary Kay Kane, *Federal Practice and Procedure* § 1839, at 175 (2d ed. 1986 & Supp. 1997) ("Wright, *et al.*"). Because, at the settlement stage, "judges no longer have the full benefit of the adversarial process," "objectors play an important role by giving courts access to information on the settlement's merits." *Bell Atlantic*, 2 F.3d at 1310.[12]

Pursuant to Rule 23.1, absent shareholders have an absolute right to appear and object to a settlement, without separately intervening pursuant to Rule 24. If their objections are rejected, these shareholders may appeal. The right of such *de facto* parties to appeal was well established at common law, and Rule 23.1 was not intended in any way to depart from that practice. To the contrary, a right to appeal is a critical component of the Rule 23.1 right to object, and a necessary counterpart to Rule 23.1's recognition of the shareholders as *de facto* parties.

By contrast, the Seventh Circuit's newly minted requirement that, as a prerequisite to appeal, objecting shareholders undertake the significant burdens associated with formal intervention has no foundation in Rule 23.1. Nor does it have any basis in the Constitution, the federal statutes governing appellate jurisdiction, or this Court's precedents. Such a requirement would, moreover, discourage shareholder participation in the settlement review process and thus undermine the goals of Rule 23.1, with-

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[12] *See also Papilsky v. Berndt*, 466 F.2d 251, 258 (2d Cir.), *cert. denied*, 409 U.S. 1077 (1972); Note, *Control over Settlement of Shareholder's Suit*, 54 Harv. L. Rev. 833 (1941); 2 George D. Hornstein, *Corporation Law and Practice* § 727 (1959); *cf. Daily Income Fund, Inc. v. Fox*, 464 U.S. 523, 532 n.7 (1984) ("[T]he provision requiring notice and court approval of settlements [is] also intended to prevent shareholders from suing in place of the corporation in circumstances where the action would disserve the legitimate interests of the company or its shareholders.").

out furthering any countervailing policies. It should be rejected.

A. Rule 23.1, This Court's Decisions, and Long-Standing Common Law Tradition Support Objectors' Right To Appeal Settlement Approvals.

1. As to one crucial point in this case, there is no dispute. It is common ground that Rule 23.1 authorizes shareholders who object to a settlement to appear in *district court* and voice their concerns without undertaking the burdens associated with formally intervening pursuant to Rule 24. That has been the repeated conclusion of the federal courts,[13] and neither the Seventh Circuit, nor the district court, nor any of the respondents here, has suggested that the objectors in this case were required to intervene in order to press their arguments before the district court. On the contrary, respondents expressly *concede* that shareholders "have the option to object [in district court] without seeking to intervene." [14]

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[13] *See, e.g., In re Pittsburgh & Lake Erie R.R. Sec. & Antitrust Litig.*, 543 F.2d 1058, 1067 (3d Cir. 1976); *Girsh v. Jepson*, 521 F.2d 153, 157, 160 (3d Cir. 1975); *White v. Auerbach*, 500 F.2d 822, 828 (2d Cir. 1974); *Cohen v. Young*, 127 F.2d 721, 724 (6th Cir. 1942); *Saylor v. Bastedo*, 594 F. Supp. 371, 373, 375 & n.3 (S.D.N.Y. 1984); *Ackert v. Ausman*, 217 F. Supp. 934, 936 (S.D.N.Y. 1963); *Webcor Elecs. v. Whiting*, 101 F.R.D. 461, 463 (D. Del. 1984); *Levin v. Mississippi River Corp.*, 59 F.R.D. 353, 367, 373 (S.D.N.Y.), *aff'd mem.*, 486 F.2d 1398 (2d Cir. 1973) (Table).

[14] Felzen Br. in Opp. 11. *See* ADM Directors Br. in Opp. 14 (similarly conceding that shareholders need not intervene in order to object in district court, but contending that, "[i]f a nonparty shareholder seeks involvement beyond that stage, intervention is the obvious next step"); ADM Brief in Opp. 17 ("Shareholder procedural rights have been provided and delineated in Rule 23.1, Federal Rules of Civil Procedure. . . . Objectors *who wish to appeal* need only intervene.") (emphasis added).

This invitation for shareholders to participate in settlement review proceedings is grounded in Rule 23.1's recognition that the rights of all shareholders will necessarily and directly be resolved in the pending derivative suit. Indeed, it is well accepted that the resolution of one derivative action against the corporation precludes any later derivative litigation arising out of the same alleged misconduct.[15] Whether they like it or not, shareholders are *de facto* parties whose rights are being adjudicated by the settlement of any derivative litigation.

Accordingly, objecting shareholders may participate in district court settlement review proceedings simply by responding to the mandatory Rule 23.1 notice; they need not intervene pursuant to Rule 24. Rule 24 is a different mechanism that may give interested shareholders rights to participate as to *other* issues relating to the derivative suit; but intervention pursuant to Rule 24 is not a requirement for those investors to be heard on the specific issue of whether a settlement that would forever bar them from bringing similar claims should be approved.

While respondents and the Seventh Circuit concede that Rule 23.1 permits a shareholder to appear and object in the district court—without intervening in the action pursuant to Rule 24—they argue that precisely the opposite is true once a case reaches a federal court of appeals. At the appellate level, in their view, only shareholders who have successfully intervened may seek relief from an erroneous district court decision to approve a derivative settlement.

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[15] *See, e.g., Nathan v. Rowan*, 651 F.2d 1223, 1226 (6th Cir. 1981); *Goldman v. Northrop Corp.*, 603 F.2d 106, 109 (9th Cir. 1979); *Cramer v. General Tel. & Elecs. Corp.*, 582 F.2d 259, 268 (3d Cir. 1978); *Reiter v. Universal Marion Corp.*, 299 F.2d 449, 452 (D.C. Cir. 1962); *Stella v. Kaiser*, 218 F.2d 64, 65 (2d Cir. 1954). *See also Matsushita Elec. Indus. Co. v. Epstein*, 516 U.S. 367, 379 (1996).

As other courts of appeals have recognized, however, such a rule would ignore the interests of objecting shareholders that Rule 23.1 was intended to protect. As *de facto* parties whose rights have been adjudicated by a derivative suit settlement, objecting shareholders must have a corresponding right to appeal. *See, e.g., In re Pittsburgh & Lake Erie R.R. Sec. & Antitrust Litig.*, 543 F.2d at 1069-70 (nonparties in derivative suit may appeal where their "equity is being diluted," since their "distinctive interests are as worthy of consideration and protection as [party] shareholders"); *United States v. LTV Corp.*, 746 F.2d 51, 54 n.5 (D.C. Cir. 1984) (nonparties may appeal from consent judgments in derivative cases because "judgments in such cases bind shareholders . . . who have received notice of the pendency of the actions").[16]

The Seventh Circuit's rule, moreover, would reverse centuries of established equitable practice that Rule 23.1 was intended to embody, not overturn. When the Federal Rules were drafted in 1938, the Advisory Committee on Civil Procedure made plain that current Rule 23.1 was based on existing law and was not designed to make any substantive changes in that law. Report of the Advisory Committee on Civil Procedure 60 (1937).[17]

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[16] The same basic rationale permits appeals by objecting class members in a Rule 23 class action. *See, e.g., Marshall v. Holiday Magic, Inc.*, 550 F.2d 1173, 1176 (9th Cir. 1977) (as class members, appellants "legal rights are affected by the settlement" and they may appeal). If anything, the case for the appellate rights of objectors is stronger in the derivative suit context because absent shareholders (unlike absent class members) have no ability to opt-out of the suit. *See infra* pp. 30-31.

[17] Courts and commenters have uniformly recognized that Rule 23.1 was intended to ratify, not change, common law practice. *See Daily Income Fund, Inc. v. Fox*, 464 U.S. at 530 ("[w]hen the Federal Rules were promulgated in 1937," prior law pertaining to derivative shareholder actions was "substantially restated"); *Cohen v. Beneficial Indus. Loan Corp.*, 337 U.S. at 548 (construing Rule 23.1 in light of prior equity rules); *Papilsky v. Berndt*, 466 F.2d 251 (same); *In re Pittsburgh & Lake Erie R.R. Spec. & Antitrust Litig.*, 543 F.2d at 1065 (same); 7C Wright, *et al.*, § 1821, at 9 (2d ed. 1986) ("The modern shareholder derivative action had its origins in equity and the content of Rule 23.1 can be traced to a number of nineteenth century decisions."); 5 James W. Moore, *Moore's Federal Practice*, § 23.1App.100, at 7 (Matthew Bender 3d ed. 1997) ("The principles of Rule 23.1 are not . . . new to federal practice. Indeed, the principles of the rule reach back well into the 19th century, thus predating the passage of the Civil Rules by several decades. When the rules were promulgated in 1937, the provisions of the Equity Rules relating to derivative actions were carried forward as original Rule 23(b)."). (footnotes omitted) (citing Equity Rule 94 (1882)).

Prior equity practice is thus directly relevant to the issue presented in this case.

Courts of equity long ago recognized that where, as here, a person's rights will necessarily be resolved by an equitable proceeding and the person has been summoned or invited to appear in court in response to an official notice, that person has *de facto* party status. Such a person may participate in trial court proceedings—and appeal—*without* undertaking the additional burdens of becoming a party. *See, e.g., Attorney General v. North Am. Life Ins. Co.*, 77 N.Y. 297, 300 (1879) (policyholders who appeared in response to court notice and objected to corporate receivership "were . . . made parties by the notice served on them" and were entitled to appeal even though "[t]here is in strictness no suit to which [they] can be made parties"); *Giffard v. Hort*, 1 Sch. & Lef. 386, 409 (Irish H. Ct. Chy. 1804) (collecting case law establishing that a variety of individuals whose rights were implicated by equitable actions "have been held entitled to re-hear the cause though not parties, because the Decree affected their interest"); *West v. Randall*, 29 Fed. Cas. 718, 723 (C.C.D.R.I. 1820) (No. 17,424) (in cases of "general right," every person affected by the decree need not be made a formal party, but rather may be considered "quasi parties to the record" who never-

theless are entitled to seek relief from the courts "if their rights are jeoparded").[18]

The English legal scholar Frederic Calvert noted in 1846 that the British common law had already provided unnamed class members the right to appeal for over 100 years. Frederic Calvert, *Observations on Suits in Equity* 38 (London, William Benning, 2d ed. 1846) (citing *Osborne v. Usher*, 6 Brown's Parliamentary Cases 20 (H. Ct. Parl. 1721)). Calvert himself defended this right at length: "[T]he privilege of appeal [in class action suits] ought to be given in such a manner as to induce the readiest acquiescence in the system of representation during the earlier part of the suit; for which reason every individual ought, as it appears to me, to . . . have the power of appealing, whether he has been a suitor . . . or by some other person as his representative." *Id.*

On this side of the Atlantic, Joseph Story similarly noted that, where affected individuals are too numerous to appear in court, "they may come in under the decree, and take the benefit of it, or show it to be erroneous, or entitle themselves to a rehearing." Joseph Story, *Commentaries on Equity Pleadings* 96 (Little, Brown, 2d ed. 1840). In sum, as one commentator recently explained after canvassing the centuries of law on this issue, a requirement that absent class members intervene in order to appeal "*has no historical foundation.*" Timothy A. Duffy, Comment, *The Appealability of Class Action Settlements by Unnamed Parties*, 60 U. Chi. L. Rev. 933, 940 (1993) (emphasis added).

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[18] *See also Cockburn v. Thompson*, 16 Ves. Jun. 321, 326-27, 33 Eng. Rep. 1005, 1007 (Ct. Ch. 1809) ("where it is impracticable to make parties, and yet the Court can by arrangement afterwards introduce the persons, as *Quasi* parties, the Court does not require, that they shall be parties on the record"); Frederic Calvert, *Parties to Suits in Equity* 62 (London, William Benning, 2d ed. 1847) ("Courts of Equity, having adopted the principle of representation in the different forms, which have been mentioned, work it out by treating the persons represented, as if they had been parties. These persons are *quasi* parties on record.").

Even more to the point, in a case decided only a few years before the Federal Rules were promulgated, this Court specifically adopted the principle that *de facto* parties' rights include the right to appeal. In *Johnson v. Manhattan Railway*, 289 U.S. 479, the Court concluded that corporate shareholders who received notice of proceedings involving a proposed temporary receivership were "*entitled*" to appear in district court—and to appeal—without taking any other steps. *Id.* at 495 (emphasis added). The Court cited in support of that proposition two lower court cases, both of which held that persons who appear in the district court in response to express court invitations need not intervene in order to appeal. *Id.* at 495 n.4, citing *Christian v. R. Hoe & Co.*, 63 F.2d 218, 218 (2d Cir. 1933) (shareholder and noteholder who objected to receivership "is rightfully here, like a defendant who is summoned by process of court and after an adverse ruling has the right to appeal"); *Mitchell v. Lay*, 48 F.2d 79, 84-85 (9th Cir. 1930), *cert. denied*, 285 U.S. 864 (1931) (appellant who did not intervene nevertheless entitled to appear and to appeal when he was "brought into court by the process of the court"). *See also Pianta v. H.M. Reich Co.*, 77 F.2d 888, 890 (2d Cir. 1935) ("There is no merit in appellees' contention that the appellant has no standing to appeal because it was not an original party to the suit and has not sought to intervene. The appellant, having appeared in opposition to the order to show cause, is like a defendant who is summoned by process of court and after an adverse ruling has the right to appeal.") (citing *Manhattan Railway* and quoting *Christian*).

In light of the Court's statement in *Manhattan Railway*, it should come as no surprise that, just a few years after the adoption of the Federal Rules, a federal appellate court squarely held that objectors in derivative actions need not intervene to appeal. *See Cohen v. Young*, 127 F.2d at 724 (citing *Manhattan Railway* in holding that objector who did not intervene is nevertheless "entitled as

of right to prosecute the appeal").[19] Indeed, these principles were once so well established that, in 1975, then-Judge Stevens, citing both *Cohen* and *Pianta*, stated unequivocally that "[t]he law is clear that a non-party shareholder who appears, pursuant to a Rule 23.1 notice, to present objections to a proposed dismissal or settlement of a derivative action may appeal an adverse decision even though he has not been formally made a party to the action." *Tryforos*, 518 F.2d at 1263 n.22.

States have also recognized these established common law principles. In particular, both Delaware and New York—States with particular expertise in applying common law principles in the modern corporate context—permit shareholders to appeal a decision approving a derivative suit settlement without intervening. *See Prezant v. DeAngelis*, 636 A.2d 915 (Del. 1994); *In re Resorts Int'l Shareholder Litig.*, 570 A.2d 259 (Del. 1990); *Geller v. Tabas*, 462 A.2d 1078 (Del. 1983); *Posen v. Cowdin*, 44 N.Y.S.2d 842, 843-44 (N.Y. App. Div. 1944); *see also Gowdey v. Commonwealth Edison Co.*, 345 N.E.2d 785, 790-91 (Ill. Ct. App. 1976); *Simons v. Horowitz*, 151 Cal. App. 3d 834, 842-44 (Cal. Ct. App. 1984); *ICSC Partners, L.P. v. Kenwood Plaza, L.P.*, 688 N.E.2d 5, 7-8 (Ohio Ct. App. 1996).

B. None of the Seventh Circuit's Arguments Supports a Requirement That Objectors Intervene in Order To Appeal.

1. Given that Rule 23.1 embodies the common law tradition permitting appeals by *de facto* parties such as

[19] *See also* 7C Wright, *et al.*, *supra*, § 1839, at 182 ("objector to the settlement may appeal the court's approval of the compromise"); 10 *Federal Procedure, Lawyers Edition* § 25:184, at 260 (1994) ("nonparty shareholder who appears, pursuant to an FRCP 23.1 notice, to present objections to a proposed dismissal or settlement of a derivative action may appeal an adverse decision without having been formally made a party to the action").

objecting shareholders, one would expect that the Seventh Circuit would not have departed from this practice without some compelling constitutional or statutory reason.

Yet no such reason exists. There is certainly no constitutional bar to permitting appeals by objecting shareholders. To have Article III standing, a person must be injured, the injury must be caused by the action at issue, and the injury must be redressable by a favorable judicial judgment. *See United States v. Hays*, 515 U.S. 737, 743 (1995). In this case, shareholders are injured when the value of their investment is reduced. That injury is caused by the district court's decision to approve a settlement that does not obtain sufficient compensation for wrongs done to the corporation. And the injury may be redressed by a court of appeals' decision reversing the district court's judgment. Indeed, Judge Easterbrook, writing for the Seventh Circuit, conceded that petitioners had standing to appeal. *See* Pet. App. 7a ("Standing means injury in fact, and a reduction in the market price of one's stock is injury.").

Nor is there any statutory basis for dismissing this appeal. The federal statute governing appeals from final district court judgments, 28 U.S.C. § 1291, simply provides that: "The courts of appeals (other than the United States Court of Appeals for the Federal Circuit) shall have jurisdiction of appeals from all final decisions of the district courts of the United States." Thus, the relevant federal statute provides no grounds to deprive petitioners of the rights historically granted to them.

2. Unable to find a constitutional or statutory basis for its rule, the Seventh Circuit rested its decision on a vast overreading of language from this Court's *per curiam* opinion in *Marino v. Ortiz*, 484 U.S. 301 (1988)—a decision that did not involve the rights of shareholders or even the related question of the rights of unnamed members of a Rule 23 plaintiff class. In particular, the court of appeals relied on the following three sentences from *Marino*:

> The rule that only parties to a lawsuit, or those that properly become parties, may appeal an adverse judgment, is well settled. . . . The Court of Appeals suggested that there may be exceptions to this general rule, primarily "when the nonparty has an interest that is affected by the trial court's judgment." We think the better practice is for such a nonparty to seek intervention for purposes of appeal.

Id. at 304 (citing *United States ex rel. Louisiana v. Jack*, 244 U.S. 397 (1917) and Federal Rule of Appellate Procedure 3(c)); *see* Pet. App. 1a-2a.

The Seventh Circuit's reliance on *Marino* is misplaced. First, unlike Rule 23.1 objectors, the persons seeking to appeal in *Marino* were not members of the plaintiff class at issue, but outsiders to the proceedings with no right to participate in the district court under Rule 23. More specifically, they were white police officers seeking to challenge a class action settlement between black officers and police authorities. Nothing in *Marino* addressed the appellate rights of persons who *are* members of the class whose rights are directly adjudicated by a judgment entered in the case and who receive a mandatory notice expressly inviting them to participate in trial court proceedings. *See Bell Atlantic*, 2 F.3d at 1308 n.6.[20]

The lone case cited in the pertinent passage of *Marino* confirms the limited nature of *Marino*'s holding—and its inapplicability here. *United States ex rel. Louisiana v. Jack* involved a land dispute between a state agency and a landowner. The State of Louisiana sought to participate in the proceedings. The Court held the State not a proper party and explained that "it has long been the law" that only "part[ies] *and priv*[*ies*] *to the record*" may appeal an adverse decision, though even to this rule the Court acknowledged some "exceptions." 244 U.S. at 402 (emphasis added); *see also Ex parte Cockcroft*, 104 U.S. 578, 579 (1882) (actual parties or ones "treated as such" by trial court may appeal); *Bayard v. Lombard*, 50 U.S. (9 How.) 530, 551 (1850) (parties and privies may appeal). Objecting shareholders are at least "privies to the record" in derivative suits and thus could appeal under the rule stated in *Louisiana* and approved in *Marino*. *See supra* pp. 19-20 (establishing that at common law such persons have been considered "*de facto*" or "*quasi*" parties).

[20] Even as to the strangers to the case at issue in *Marino*, the Court merely purported to establish "better practice," not an exceptionless rule. *See* 484 U.S. at 304.

That the Seventh Circuit's understanding of *Marino* is untenable is further established by the unlikely consequences that would follow from the court of appeals' reading of that case. If *Marino* did *hold* that "only parties to a lawsuit, or those that properly become parties, may appeal" (484 U.S. at 304), an enormous body of settled law would have been overturned by a single phrase in that *per curiam* opinion. Nonparties whose rights are adjudicated by trial court judgments are treated by the federal courts as *de facto* parties and permitted to appeal without intervention in a wide range of circumstances. *See* 15A Wright, *et al.*, *supra*, § 3902.1, at 102 (2d ed. 1992 & Supp. 1998).[21] For instance, federal courts routinely permit nonparty appeals from judgments that bind the nonparty by name. *Id.* at 122 (citing cases).[22] Courts permit nonparty witnesses held

[21] *See id.* at 122 (collecting examples) ("Nonparties need not always go through a formal intervention procedure to achieve standing to appeal. Appeals have been permitted on showings that range from easy cases in which a nonparty is formally addressed by a court order through less clear cases in which a nonparty is significantly affected.").

[22] *See also Class Plaintiffs v. City of Seattle*, 955 F.2d 1268, 1277-78 (9th Cir.), *cert. denied*, 506 U.S. 953 (1992); *United States v. International Bhd. of Teamsters*, 931 F.2d 177, 183-84 (2d Cir. 1991); *Hoxworth v. Blinder, Robinson & Co.*, 903 F.2d 186, 194 n.12 (3d Cir. 1990); *EEOC v. Pan American World Airways, Inc.*, 897 F.2d 1499, 1504 (9th Cir.), *cert. denied*, 498 U.S. 815 (1990); *Hal Roach Studios, Inc. v. Richard Feiner & Co.*, 896 F.2d 1542,

in contempt for refusing discovery to appeal on claims of privilege, lack of personal jurisdiction, and other matters. *See* 15A Wright, *et al., supra,* § 3902.1, at 124.[23] They regularly allow attorneys and expert witnesses to appeal district court denials of fees. *See* 15A Wright, *et al., supra,* at 126 & n.45.[24] And non parties obligated to reimburse the defendant for amounts paid under the trial court's judgment are also heard on a routine basis. *See* 15A Wright, *et al., supra,* § 3902.1 at 127 & n.47.[25]

Faced with this enormous body of contrary case law, even respondents have declined to defend the Seventh Circuit's understanding that *Marino* stands for the bald

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1546-47 (9th Cir. 1989), *cert. denied*, 498 U.S. 815 (1990); *SEC v. Wencke*, 783 F.2d 829, 834 (9th Cir.), *cert. denied*, 479 U.S. 818 (1986); *In re Baldwin-United Corp.*, 770 F.2d 328, 335 (2d Cir. 1985); *In re Grand Jury Proceedings*, 654 F.2d 268, 270-71 (3d Cir.), *cert. denied*, 454 U.S. 1098 (1981); *Thompson v. Freeman*, 648 F.2d 1144, 1147 n.5 (8th Cir. 1981); *Commercial Sec. Bank v. Walker Bank & Trust Co.*, 456 F.2d 1352, 1354 (10th Cir. 1972).

[23] *See also United States Catholic Conference v. Abortion Rights Mobilization, Inc.*, 487 U.S. 72, 76 (1988); *General Ins. Co. of Am. v. Eastern Consolidated Utils., Inc.*, 126 F.3d 215, 218 (3d Cir 1997); *United States v. Bertoli*, 994 F.2d 1002, 1012 (3d Cir. 1993); *Petersen v. Douglas County Bank & Trust Co.*, 967 F.2d 1186, 1188 (8th Cir. 1992); *Port Drum Co. v. Umphrey*, 852 F.2d 148, 150 n.2 (5th Cir. 1988); *Norwood v. Slammons*, 788 F. Supp. 1020, 1024 (W.D. Ark. 1991).

[24] *See also United States v. Tippett*, 975 F.2d 713, 718 (10th Cir. 1992); *Price v. Pelka*, 690 F.2d 98, 102 (6th Cir. 1982); *James v. Home Constr. Co. of Mobile, Inc.*, 689 F.2d 1357, 1359 (11th Cir. 1982); *Lipscomb v. Wise*, 643 F.2d 319, 320-21 (5th Cir. 1981); *Dietrich Corp. v. King Resources Co.*, 596 F.2d 422, 424 (10th Cir. 1979); *Preston v. United States*, 284 F.2d 514, 515 n.1 (9th Cir. 1960); *Angoff v. Goldfine*, 270 F.2d 185, 186 (1st Cir. 1959).

[25] *See also Fields v. Blum*, 629 F.2d 825, 827 (2d Cir. 1980) (order enjoining reduction of welfare benefits by city official could be appealed by State, since State was legally required to reimburse city for payments and controlled both the activities complained of and the conduct of local officials).

proposition that "only parties may appeal." Pet. App. 3a. Respondents' alternative understanding of *Marino*—an understanding that has no basis in the text of that decision—is that an ill-defined, but limited subset of nonparties who are "personally addressed" by trial court orders may also appeal. *See* ADM Br. in Opp. 14 n.6; ADM Directors Br. in Opp. 17. Respondents have cited no decision from any court establishing such a rule, and we are not aware of any.

Indeed, the limited scope of respondents' proffered rule is inconsistent with common law practice permitting unnamed class members to appeal (*see supra*); with this Court's long-standing jurisprudence allowing *all* "priv[ies] to the record" to appeal (*Louisiana*, 244 U.S. at 402); and with federal appellate practice, which has routinely permitted unnamed privy nonparty appeals. *See, e.g., supra* note 25 (unnamed persons legally liable to reimburse defendant for amounts paid in judgment permitted to appeal); 15A Wright, *et al., supra,* § 3902.1, at 122 (named nonparty presents "easiest" but not exclusive case for appeal); *id.* at 126 (though order does not "bind a nonparty by name," the nonparty may appeal when order has "[o]bvious and important effects" on him).[26]

Moreover, even if respondents' rule did have some basis in law, they have thus far failed to explain how it would forbid appeals by shareholders who, like petitioners, have their objections specifically overruled—and thus "person-

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[26] Federal court practice on this point is so deeply rooted that several courts of appeals have established a three-part standing test governing the general question whether nonparties may appeal. *See, e.g., Krebs Chrysler-Plymouth, Inc. v. Valley Motors, Inc.*, 141 F.3d 490, 496 (3d Cir. 1998); *Searcy v. Philips Elecs. N. Am. Corp.*, 117 F.3d 154, 157-58 (5th Cir. 1997); *see also Keith v. Volpe*, 118 F.3d 1386, 1391 (9th Cir. 1997).

ally addressed"—by the trial court order approving the settlement.[27]

3. Beyond *Marino*, the only other authority the Seventh Circuit cited to support its decision to bar all nonparty appeals is Federal Rule of Appellate Procedure 3(c). Pet. App. 2a. Rule 3(c), the panel noted, provides that "[a] notice of appeal must specify the *party or parties* taking the appeal by naming each appellant in either the caption or the body of the notice of appeal" (emphasis added). Since no party is taking the appeal here, the Seventh Circuit reasoned, it must be improper under Rule 3(c). *Id.*

Rule 3(c) cannot come close to bearing the weight that the Seventh Circuit placed upon it. Again, the Seventh Circuit's reading of Rule 3(c) would bar not just nonparty shareholder appeals, but *all* nonparty appeals —an improbable result that would effectively overrule innumerable decisions, from both before and after Rule 3(c), that had never before been controversial. *See supra* notes 20-26. As noted, that action would be so extraordinary that even respondents do not urge it here.

In any event, contrary to the Seventh Circuit's conclusion (Pet. App. 7a), the Federal Rules of Appellate Procedure are *not* intended to limit the jurisdiction of the courts of appeals over appeals from final district court judgments; that is the function of Article III and section 1291, neither of which poses any obstacle to appeal here. Federal Rule of Appellate Procedure 1(b) states in no uncertain terms that "[t]hese rules *shall not be construed to extend or limit the jurisdiction of the courts of appeals*

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[27] *See* Hearing Tr. 79 (July 7, 1997) (R.103) ("All right. The court's ready to rule. Having heard the remarks of the proponents of the settlement and the remarks of those in opposition [*i.e.*, petitioners], the court concludes that the settlement, which is before the court is fair, reasonable, and adequate.").

as established by law" (emphasis added). The Seventh Circuit's reliance on Rule 3(c) in this context cannot be squared with the plain language of that Rule.

Consistent with the principle that Rule 3(c) does not limit the courts of appeals' jurisdiction, the language of that provision does not even purport to delineate who is eligible to appeal. Rather, as its title suggests, Rule 3(c) is concerned only with the formal "*content*[*s*] of the notice of appeal" filed by otherwise eligible appellants (emphasis added). Rule 3(c) simply ensures that sufficient information appears on the face of the notice for the court of appeals to discern the issues and litigants before it:

> (c) *Content of the Notice of Appeal.*—A notice of appeal must specify the party or parties taking the appeal by naming each appellant in either the caption or the body of the notice of appeal. An attorney representing more than one party may fulfill this requirement by describing those parties with such terms as "all plaintiffs," "the defendants," "the plaintiffs A, B, et al.," or "all defendants except X." . . .

Fed. R. App. P. 3 (c).

Nor is there any indication that Rule 3(c)'s drafters ever intended it to exclude the possibility of nonparty appeals. To the contrary, the 1967 advisory committee notes indicate that the Rule "merely restate[s], in modified form, provisions now found in the civil and criminal rules . . . and decisions under the present rules which *dispense with literal compliance in cases in which it cannot fairly be exacted should control interpretation of these rules.*" Fed. R. App. P. 3(c) 1967 advisory committee note (emphasis added). The 1979 advisory committee notes reemphasize the same point. *See id.* 1979 advisory committee note ("so long as the function of notice is met by the filing of a paper indicating an inten-

tion to appeal, the substance of the rule has been complied with").[28]

4. The Seventh Circuit's final argument is that the case for allowing appeals from settlement approvals by objecting shareholders in Rule 23.1 actions is weaker than the case (which the Seventh Circuit had already rejected) for allowing such appeals by unnamed class members in Rule 23 actions. *See* Pet. App. 4a-5a.

As an initial matter, the premise of that argument—that objecting class members cannot appeal—is itself wrong. In any event, the unfavorable comparison between objecting shareholders and unnamed class members is directly at odds with the judicial and legislative judgment that the two groups should be granted the same rights. The language of Rule 23.1 tracks the language of Rule 23(e) granting class members the right to object to proposed settlements.[29] Until 1966, when Rule 23.1 was broken out into a separate rule, derivative actions were considered a form of class actions governed by what was then Rule 23(b). 7A Wright, *et al.*, *supra*, § 1752, at 18 (1986). And, as the identity of the language used by Rules 23(e) and 23.1 suggests, that division was in no way intended to grant lesser rights to objecting shareholders than objecting class members. On the contrary, in proposing this change, the

[28] The fact that Rule 3(c) was not intended to preclude appeals by nonparties is further underscored by Rule 3(b), which speaks simply of "*persons* . . . entitled to appeal from a judgment or order of a district court." (emphasis added).

[29] *Compare* Rule 23(e) ("A class action shall not be dismissed or compromised without the approval of the court, and notice of the proposed dismissal or compromise shall be given to all members of the class in such manner as the court directs.") *with* Rule 23.1 ("The action shall not be dismissed or compromised without the approval of the court, and notice of the proposed dismissal or compromise shall be given to shareholders or members in such manner as the court directs.").

Advisory Committee specifically noted that the "mandatory notice" requirement contained in old Rule 23 "was *primarily directed* to derivative actions by shareholders" and was "continued for such actions by Rule 23.1." Preliminary Draft of Proposed Amendments to the Rules of Civil Procedure 114 (1964) (citing *Cunningham v. English*, 269 F.2d 539 (D.C. Cir. 1959)) (emphasis added).

Similarly, the Seventh Circuit's suggestion that individual shareholders, unlike individual class members, are not "injured part[ies]" who are "entitled to litigate" these issues simply reverses the judgment reflected on the face of Rule 23.1. Pet. App. 5a. By explicitly authorizing derivative suits by aggrieved shareholders, Rule 23.1 confirms that shareholders *are* sufficiently injured by corporate action to invoke the jurisdiction of the federal courts. Put differently, what Rule 23.1 does is precisely to grant shareholders an "entitle[ment]" to litigate in federal court, subject only to the specific safeguards enumerated in the Rule itself.

Moreover, because *all* investors will be bound by the result in the action being settled, each investor's rights will necessarily be implicated by a decision to approve the settlement and each investor's entitlement will thus be affected. In this respect, the case for allowing shareholders to appeal is *stronger* than that for class members, because shareholders do not have the option available to many unnamed class members of opting-out of a settlement they do not believe is fair. *See Gottlieb*, 11 F.3d at 1011 (concluding that case for Rule 23.1 nonparty appeals was more persuasive because "there is no opt-out provision in shareholder derivative suits"); *Rosenbaum v. McAllister*, 64 F.3d at 1442 (same).[30]

[30] The Seventh Circuit's suggestion that shareholders can obtain relief by altering the composition of the corporate board of directors (Pet. App. 5a) ignores the fact that derivative suits are a mecha-

C. An Intervention Requirement Would Create Significant Disincentives to Objector Participation Without Serving any Countervailing Purposes.

Objecting shareholders play a critical role in ensuring the fairness of derivative suit settlements. Once plaintiffs' counsel and the defendants have reached a tentative settlement, their strong common interest is in obtaining approval for that settlement. Settlement hearings thus frequently devolve into "jointly orchestrated" "pep rallies" in which no party questions the fairness of the settlement. Jonathan R. Macey and Geoffrey P. Miller, *The Plaintiff's Attorney's Role in Class Action and Derivative Litigation: Economic Analysis and Recommendations for Reform*, 58 U. Chi. L. Rev. 1, 46 (1991).

Only objecting shareholders can give a federal court the benefit of an adversarial presentation as to whether a particular settlement is "fair and adequate" and thus should be approved. *See Bell Atlantic*, 2 F.3d at 1310 ("[o]bjectors play an important role by giving courts access to information on the settlement's merits," especially because "judges no longer have the full benefit of the adversarial process"); *Cohen v. Young*, 127 F.2d at 725 (nonparty shareholder participation is crucial so "that the court may have the full benefit of that broader information which comes from receiving advice as to the views of all parties concerned").[31]

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nism for obtaining relief when a *minority* of shareholders cannot spur a board to act and thus must seek other means of redress. *See* Rule 23.1 (mandating that derivative plaintiff demonstrate that it has made a demand on the board and explain the reason for "plaintiff's failure to obtain . . . action" from the board).

31 Objecting shareholders also serve the additional function of providing needed information to financial markets. *Cf. Musick, Peeler & Garrett v. Employees Ins. of Wausau*, 508 U.S. 286, 296 (1993) (explaining that SEC Rule 10(b)(5) serves valuable goals of deterring fraud and "ensur[ing] full disclosure of information

Objecting shareholders perform this same function on appeal. Requiring intervention as a prerequisite for such appeals would dramatically decrease their number and thereby impair the ability of objecting shareholders to serve the recognized public function of exposing, defeating, and deterring collusive or inadequate settlements. Yet neither respondents nor the Seventh Circuit have identified *any* benefit from such a judicially manufactured rule.

1. There is no question that objecting shareholders serve an important function on appeal. Appellate review is an essential component of shareholder participation because it provides a strong incentive for district courts to consider shareholder objections fully and a direct avenue for correcting district court errors. *See* Hon. Jon O. Newman, *A Study of Appellate Reversals*, 58 Brooklyn L. Rev. 629, 633 (1992) (reporting reversal rate in civil cases of 27 percent); Steven A. Childress & Martha Davis, *Federal Standards of Review: Trial to the Court* § 2.14, at 2-103 (2d ed. 1982) (reporting civil reversal rate of approximately 16 percent for 1988-1989).

Shareholder appeals in particular have yielded tangible benefits for the corporation. For example, the court of appeals in *Rosenbaum, supra*, held that nonparty shareholders could appeal attorney fee awards and remanded for reconsideration of the $2.6 million fee award. "As a direct result," the district court subsequently ordered $1.4 million returned to the corporation. Order, *Rosenbaum v. McAllister*, Civil Case No. 91-B-2164 (D. Colo. Feb. 14, 1997). *See also In re Pittsburgh & Lake Erie*

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material to investment decisions"). Adversarial scrutiny by objectors provides information necessary for market participants to assess rationally the real economic value of any settlement to the company and its stock. For instance, in this case, objecting shareholders exposed the speciousness of plaintiffs' claims that they had added $158 million in value through corporate governance reforms. *See supra* p. 7.

R.R. Sec. Antitrust Litig., 543 F.2d 1058 (holding that settlement's diversion of value from the corporation to the plaintiffs and their attorneys was so egregiously unfair that district court's approval constituted an abuse of discretion); *Ficalora v. Lockheed California Co.*, 751 F.2d 995, 997 (9th Cir. 1985) (remanding case for "reasoned judgment" that the settlement "is not the product of fraud or overreaching by, or collusion among, the negotiating parties").

2. There is also no question that requiring intervention would sharply curtail, if not eliminate, shareholder appeals and correspondingly impair the public functions they serve. The legal hurdles to intervention by objecting shareholders at the settlement phase are daunting. Rule 24(b) requires motions to intervene to be "timely." Under existing case law, there is a presumption that motions made after a tentative settlement has been reached fail that test.[32] And that is not a problem that is within the power of dissenting shareholders to fix. Shareholders are first notified of an ongoing derivative lawsuit under Rule 23.1 only *after* a settlement has been struck. *See* Fed. R. Civ. P. 23.1.[33] "Thus, even if they were to request intervention immediately after learning of the litigation . . . the court might very well find their request to be 'untimely.'" Kim, 66 Tenn. L. Rev. at ——.

Unnamed shareholders seeking to intervene under Rule 24(a) must also convince the district court that their interests are not "adequately represented" by the existing named shareholders. *Id.* at —. Yet, in allowing the action to proceed pursuant to Rule 23.1, the court has necessarily already found that the named shareholder-plaintiff *does* "adequately represent" the interests of shareholders generally. *Id.* In such circumstances, "representation will be presumed adequate" and intervention virtually impossible. 7C Wright, *et al.*, *supra*, § 1909, at 324; *cf. Sam Fox Publ'g Co. v. United States*, 366 U.S. 683, 691-92 (1961). Indeed, some lower courts have suggested that, as a matter of law, objecting shareholders' interests are "adequately protected" by shareholder-plaintiffs. *See In re General Tire & Rubber Co. Sec. Litig.*, 726 F.2d 1075, 1087 (6th Cir.), *cert. denied*, 469 U.S. 858 (1984).

3 Even if objecting shareholders could (somehow) clear the legal hurdles to intervention, they would still face enormous practical disincentives. Indeed, there are *already* significant financial disincentives to shareholder participation of any sort. Objectors receive no direct financial compensation for their activities, and no guarantee of lucrative attorneys' fees awards even if they succeed in convincing a court not to approve a settlement. They participate in derivative proceedings only for whatever incremental *pro rata* value might accrue to their individual stock holdings as a result of their efforts. *Bell Atlantic*, 2 F.3d at 1309 ("shareholders . . . lack the incentive . . . to police settlements [because] the costs of policing typically outweigh any *pro rata* benefits to the shareholder"). Meanwhile, objectors shoulder the substantial costs of hiring counsel, analyzing settlement materials, filing written objections, and appearing in court, all within a matter of days or weeks. Even the largest institutional shareholders only rarely have the incentive—and the means—to participate. *See* Remarks of District Judge Vaughn R. Walker, ABA National Securities Litigation Institute at 7-8 (June 5, 1998) ("[I]nstances of institutional investors actively leading a [securities class] litigation effort remain relatively rare. . . . This is no surprise. . . . [I]n-

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[32] *See, e.g., Ragsdale v. Turnock*, 941 F.2d 501, 504 (7th Cir. 1991) ("[t]he prejudice to the present parties . . . is obvious and substantial"; "'intervention at this time would render worthless all of the parties' painstaking negotiations'"), *cert. denied*, 502 U.S. 1035 (1992); *Farmland Dairies v. Commissioner of New York State Dep't of Agric. & Markets*, 847 F.2d 1038, 1043-44 (2d Cir. 1988); *Jones v. Caddo Parish Sch. Bd.*, 735 F.2d 923, 926 (5th Cir. 1984).

[33] The settlement in this case had already been tentatively "approved" by the district court before notice was provided. *See supra* p. 7.

stitutional investors have disincentives to becoming [parties]. . . . Lawsuits are costly in time, money and other resources.").

Requiring intervention would extinguish even the modest incentives that now exist for shareholder appeals. Shareholders wishing to preserve a right to appeal would face the added financial burden of drafting a pleading the equivalent of a complaint (expressly required by Rule 24) and litigating the timeliness of their motion and the adequacy of existing representation. They would also face all the costs and burdens associated with party status, including wide-ranging Rule 26(a)(1) automatic disclosure duties and the obligation to respond to interrogatories, appear for depositions, and answer virtually unlimited demands for documents.[34]

In addition, shareholders who receive notice under Rule 23.1 would be forced to make a snap decision (within four weeks here) not just whether to participate, but also whether to accept the burdens associated with party status. Institutional shareholders—those who are the most likely to have enough at stake to make participation economical—simply cannot make such decisions that quickly, because of the need to consult their boards of directors. *See* Weiss & Beckerman, 104 Yale L.J. at 2100 ("[l]ack of timely notice makes it difficult for institutional investors to participate in class actions"). Indeed, Congress has expressly recognized that such quick

[34] *Cf.* Joseph A. Grundfest & Michael A. Perino, *The Pentium Papers: A Case Study of Collective Institutional Investor Activism in Litigation*, 38 Ariz. L. Rev. 559, 562 (1996) ("[f]ormal participation and its attendant litigation cost and risk may . . . be an unnecessarily complex and expensive means for institutional investors to express their views on the merits of class action or derivative litigation"); Elliott J. Weiss & John S. Beckerman, *Let the Money Do the Monitoring: How Institutional Shareholders Can Reduce Agency Costs in Securities Class Actions*, 104 Yale L.J. 2053, 2103-05 (1995) (discussing barriers imposed by intervention).

deadlines make institutional shareholders participation unduly and undesirably difficult.[35]

4. Respondents fleetingly suggest that requiring intervention as a prerequisite to appeal serves the purpose of weeding out frivolous appeals, thereby enhancing judicial efficiency. ADM Br. in Opp. 18 n.12. But they can present no evidence that the courts of appeals are in need of such protection. The substantial costs associated with objecting and appealing *already* deter meaningful shareholder participation in all but the most obvious cases of abuse.

Petitioners have been able to locate in LEXIS, since 1990, only 12 federal derivative suit settlements, not including this one, that attracted one or more objectors in district court.[36] We have been able to locate (again excluding the instant case) only 4 objector appeals from

[35] In the 1995 Private Securities Litigation Reform Act, Congress expressly recognized that institutional shareholders are the most likely to represent the interests of shareholders generally and thus to prevent collusion, and accordingly changed many of the procedural rules associated with securities class actions to make their participation easier. *See* 15 U.S.C. § 78u-4(a)(3)(A)(i) (requiring notice period after filing of Rule 23 securities class action complaint to allow time for potential lead plaintiffs to come forward); H.R. Conf. Rep. No. 104-369, at 34 (1995) (explaining that "[t]he Conference Committee believes that increasing the role of institutional investors in class actions will ultimately benefit shareholders and assist courts by improving the quality of representation in securities class actions"; decrying fact that "current system often works to prevent institutional shareholders" from participating in class actions; and stating that "the Conference Committee seeks to increase the likelihood that institutional investors will" participate by, *inter alia*, providing sufficiently long notice periods to enable institutional shareholders time to convene their boards and decide to come forward as potential lead plaintiffs).

[36] *See Rosenbaum*, 64 F.3d 1439; *Bell Atlantic*, 2 F.3d 1304; *Granada Invs., Inc. v. DWG Corp.*, 962 F.2d 1203 (6th Cir. 1992); *Ackerman v. Kassar*, No. 91-56521, 1993 U.S. App. LEXIS

Rule 23.1 derivative suit settlements since 1990.[37] Despite decades of common law, federal, and state practice permitting objector appeals, petitioners are unable to locate a single court or commentator complaining about the manageability of objector appeals in derivative suits. There simply is no problem to which the Seventh Circuit's proposed rule is a solution.

In fact, mandating intervention would impose *more* work on the federal courts, not less. The district court would have to litigate and resolve a motion to intervene as well as a settlement hearing. *See Webcor Elecs.*, 101 F.R.D. at 463 (complaining that Rule 24 motion to intervene was "superfluous procedural question" since non-party objector was already an invited Rule 23.1 participant in litigation). If intervention is denied, the court of appeals must still hear an appeal. Its attention is merely shifted to the motion to intervene, and away from the merits of the settlement and the policy goals that objecting shareholder participation was designed to serve.

22074 (9th Cir. Aug. 26, 1998); *In re Texaco, Inc. Shareholder Litig.*, No. 96 Civ. 8343, 1998 U.S. Dist. LEXIS 15027 (S.D.N.Y. Sept. 15, 1998); *Osher v. SCA Realty I, Inc.*, 945 F. Supp. 298 (D.D.C. 1996); *In re Fleet/Norstar Fin. Sec. Litig.*, 935 F. Supp. 99 (1996), *opinion supplemented on other grounds*, 974 F. Supp. 155 (D.R.I. 1997); *In re Chambers Dev. Sec. Litig.*, 912 F. Supp. 822 (W.D. Pa. 1995); *In re First Investors Corp. Sec. Litig.*, No. 90 Civ. 7225, *et al.*, 1993 U.S. Dist. LEXIS 18044 (S.D.N.Y. Dec. 22, 1993); *Fischer & Porter Co. v. Tolson*, No. 91-7822, 1993 U.S. Dist. LEXIS 11481 (Aug. 18, 1993), *amended on other grounds*, 1993 U.S. Dist. LEXIS 14719 (E.D. Pa. Oct. 19, 1993); *Harkness Apartment Owners Corp. v. FDIC*, No. 87 Civ. 7080, 1993 U.S. Dist. LEXIS 10499 (S.D.N.Y. July 30, 1993); *In re Centocor, Inc. Sec. Litig.*, No. 92-CV-1071, 1993 U.S. Dist. LEXIS 7229 (E.D. Pa. June 2, 1993).

[37] *See Rosenbaum*, 64 F.3d 1439; *Bell Atlantic*, 2 F.3d 1304; *Granada Invs., Inc.*, 962 F.2d 1203; *Ackerman*, 1993 U.S. App. LEXIS 22074.

5. Some of the respondents have intimated that the disincentives created by an intervention requirement might be alleviated by judicially created rules mandating that intervention motions always be granted in this particular context and excepting shareholder intervenors from *any* of the normal obligations associated with party status. ADM Br. in Opp. 16; ADM Directors' Br. in Opp. 14-15 & n.2. Shareholders would only need to comply with a procedural formality to protect their right to appeal.

But the Court would have to change Rule 24 intervention law radically for objecting shareholders in order to ensure that an intervention requirement does not undermine the policies of Rule 23.1. The Court would have to make new law on the timeliness of an intervention motion and the adequacy of existing representation. It would also need to absolve shareholders from drafting a pleading the equivalent of a complaint, as well as from Rule 26(a)(1)'s automatic disclosure duties and the various discovery obligations that follow from intervention.

Even if the Court could do all this, the question remains, what would be gained by such a watered-down intervention requirement? The answer is: nothing. No substantive purpose would be served, and the courts would be burdened with needless paperwork, all so that objectors could obtain a stamp on their passport that allows them to proceed to an appellate court. The Court should not take it upon itself to manufacture any such limitation on access to the federal courts of appeals.

There is no constitutional or statutory basis for respondents' proposed intervention requirement. It runs directly contrary to centuries of common law precedent embodied in Rule 23.1 and finds no support anywhere in the Federal Rules or this Court's cases. It would also undermine the important and recognized role of objecting shareholders in exposing collusive settlements. It should be rejected.

CONCLUSION

The Seventh Circuit's order dismissing petitioners' appeal should be reversed.

Respectfully submitted,

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November 10, 1998

ADDENDUM

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28 U.S.C. § 1291. Final decisions of district courts

The courts of appeals (other than the United States Court of Appeals for the Federal Circuit) shall have jurisdiction of appeals from all final decisions of the district courts of the United States, the United States District Court for the District of the Canal Zone, the District Court of Guam, and the District Court of the Virgin Islands, except where a direct review may be had in the Supreme Court. The jurisdiction of the United States Court of Appeals for the Federal Circuit shall be limited to the jurisdiction described in sections 1292(c) and (d) and 1295 of this title.

Federal Rule of Appellate Procedure 1. Scope of Rules and Title

(a) Scope of Rules. These rules govern procedure in appeals to United States courts of appeals from the United States district courts and the United States Tax Court; in appeals from bankruptcy appellate panels; in proceedings in the courts of appeals for review or enforcement of orders of administrative agencies, boards, commissions and officers of the United States; and in applications for writs or other relief which a court of appeals or a judge thereof is competent to give. When these rules provide for the making of a motion or application in the district court, the procedure for making such motion or application shall be in accordance with the practice of the district court.

(b) Rules Not to Affect Jurisdiction. These rules shall not be construed to extend or limit the jurisdiction of the courts of appeals as established by law.

(c) Title. These rules may be known and cited as the Federal Rules of Appellate Procedure.

Federal Rule of Appellate Procedure 3. Appeal as of Right—How Taken

(a) Filing the Notice of Appeal. An appeal permitted by law as of right from a district court to a court of appeals must be taken by filing a notice of appeal with the clerk of the district court within the time allowed by Rule 4. At the time of filing, the appellant must furnish the clerk with sufficient copies of the notice of appeal to enable the clerk to comply promptly with the requirements of subdivision (d) of this Rule 3. Failure of an appellant to take any step other than the timely filing of a notice of appeal does not affect the validity of the appeal, but is ground only for such action as the court of appeals deems appropriate, which may include dismissal of the appeal. Appeals by permission under 28 U.S.C.

§ 1292(b) and appeals in bankruptcy must be taken in the manner prescribed by Rule 5 and Rule 6 respectively.

(b) Joint or Consolidated Appeals. If two or more persons are entitled to appeal from a judgment or order of a district court and their interests are such as to make joinder practicable, they may file a joint notice of appeal, or may join in appeal after filing separate timely notices of appeal, and they may thereafter proceed on appeal as a single appellant. Appeals may be consolidated by order of the court of appeals upon its own motion or upon motion of a party, or by stipulation of the parties to the several appeals.

(c) Content of the Notice of Appeal.—A notice of appeal must specify the party or parties taking the appeal by naming each appellant in either the caption or the body of the notice of appeal. An attorney representing more than one party may fulfill this requirement by describing those parties with such terms as "all plaintiffs," "the defendants," "the plaintiffs A, B, et al.," or "all defendants except X." A notice of appeal filed pro se is filed on behalf of the party signing the notice and the signer's spouse and minor children, if they are parties, unless the notice of appeal clearly indicates a contrary intent. In a class action, whether or not the class has been certified, it is sufficient for the notice to name one person qualified to bring the appeal as representative of the class. A notice of appeal also must designate the judgment, order, or part thereof appealed from, and must name the court to which the appeal is taken. An appeal will not be dismissed for informality of form or title of the notice of appeal, or for failure to name a party whose intent to appeal is otherwise clear from the notice. Form 1 in the Appendix of Forms is a suggested form for a notice of appeal.

(d) Serving the Notice of Appeal.—The clerk of the district court shall serve notice of the filing of a notice of appeal by mailing a copy to each party's counsel of record

(apart from the appellant's), or, if a party is not represented by counsel, to the party's last known address. The clerk of the district court shall forthwith send a copy of the notice and of the docket entries to the clerk of the court of appeals named in the notice. The clerk of the district court shall likewise send a copy of any later docket entry in the case to the clerk of the court of appeals. When a defendant appeals in a criminal case, the clerk of the district court shall also serve a copy of the notice of appeal upon the defendant, either by personal service or by mail addressed to the defendant. The clerk shall note on each copy served the date when the notice of appeal was filed and, if the notice of appeal was filed in the manner provided in Rule 4(c) by an inmate confined in an institution, the date when the clerk received the notice of appeal. The clerk's failure to serve notice does not affect the validity of the appeal. Service is sufficient notwithstanding the death of a party or the party's counsel. The clerk shall note in the docket the names of the parties to whom the clerk mails copies, with the date of mailing.

(e) Payment of Fees.—Upon the filing of any separate or joint notice of appeal from the district court, the appellant shall pay to the clerk of the district court such fees as are established by statute, and also the docket fee prescribed by the Judicial Conference of the United States, the latter to be received by the clerk of the district court on behalf of the court of appeals.

Federal Rule of Civil Procedure 23. Class Actions

(a) Prerequisites to a Class Action. One or more members of a class may sue or be sued as representative parties on behalf of all only if (1) the class is so numerous that joinder of all members is impracticable, (2) there are questions of law or fact common to the class, (3) the claims or defenses of the representative parties are typical of the claims or defenses of the class, and (4) the representative parties will fairly and adequately protect the interests of the class.

(b) Class Actions Maintainable. An action may be maintained as a class action if the prerequisites of subdivision (a) are satisfied, and in addition:

(1) the prosecution of separate actions by or against individual members of the class would create a risk of

(A) inconsistent or varying adjudications with respect to individual members of the class which would establish incompatible standards of conduct for the party opposing the class, or

(B) adjudications with respect to individual members of the class which would as a practical matter be dispositive of the interests of the other members not parties to the adjudications or substantially impair or impede their ability to protect their interests; or

(2) the party opposing the class has acted or refused to act on grounds generally applicable to the class, thereby making appropriate final injunctive relief or corresponding declaratory relief with respect to the class as a whole; or

(3) the court finds that the questions of law or fact common to the members of the class predominate over any questions affecting only individual members, and that a class action is superior to other

available methods for the fair and efficient adjudication of the controversy. The matters pertinent to the findings include: (A) the interest of members of the class in individually controlling the prosecution or defense of separate actions; (B) the extent and nature of any litigation concerning the controversy already commenced by or against members of the class; (C) the desirability or undesirability of concentrating the litigation of the claims in the particular forum; (D) the difficulties likely to be encountered in the management of a class action.

(c) Determination by Order Whether Class Action to be Maintained; Notice; Judgment; Actions Conducted Partially as Class Actions.

(1) As soon as practicable after the commencement of an action brought as a class action, the court shall determine by order whether it is to be so maintained. An order under this subdivision may be conditional, and may be altered or amended before the decision on the merits.

(2) In any class action maintained under subdivision (b)(3), the court shall direct to the members of the class the best notice practicable under the circumstances, including individual notice to all members who can be identified through reasonable effort. The notice shall advise each member that (A) the court will exclude the member from the class if the member so requests by a specified date; (B) the judgment, whether favorable or not, will include all members who do not request exclusion; and (C) any member who does not request exclusion may, if the member desires, enter an appearance through counsel.

(3) The judgment in an action maintained as a class action under subdivision (b)(1) or (b)(2), whether or not favorable to the class, shall include and describe those whom the court finds to be members of the class.

The judgment in an action maintained as a class action under subdivision (b)(3), whether or not favorable to the class, shall include and specify or describe those to whom the notice provided in subdivision (c)(2) was directed, and who have not requested exclusion, and whom the court finds to be members of the class.

(4) When appropriate (A) an action may be brought or maintained as a class action with respect to particular issues, or (B) a class may be divided into subclasses and each subclass treated as a class, and the provisions of this rule shall then be construed and applied accordingly.

(d) Orders in Conduct of Actions. In the conduct of actions to which this rule applies, the court may make appropriate orders: (1) determining the course of proceedings or prescribing measures to prevent undue repetition or complication in the presentation of evidence or argument; (2) requiring, for the protection of the members of the class or otherwise for the fair conduct of the action, that notice be given in such manner as the court may direct to some or all of the members of any step in the action, or of the proposed extent of the judgment, or of the opportunity of members to signify whether they consider the representation fair and adequate, to intervene and present claims or defenses, or otherwise to come into the action; (3) imposing conditions on the representative parties or on intervenors; (4) requiring that the pleadings be amended to eliminate therefrom allegations as to representation of absent persons, and that the action proceed accordingly; (5) dealing with similar procedural matters. The orders may be combined with an order under Rule 16, and may be altered or amended as may be desirable from time to time.

(e) Dismissal or Compromise. A class action shall not be dismissed or compromised without the approval of the court, and notice of the proposed dismissal or com-

promise shall be given to all members of the class in such manner as the court directs.

Federal Rule of Civil Procedure 23.1. Derivative Actions by Shareholders

In a derivative action brought by one or more shareholders or members to enforce a right of a corporation or of an unincorporated association, the corporation or association having failed to enforce a right which may properly be asserted by it, the complaint shall be verified and shall allege (1) that the plaintiff was a shareholder or member at the time of the transaction of which the plaintiff complains or that the plaintiff's share or membership thereafter devolved on the plaintiff by operation of law, and (2) that the action is not a collusive one to confer jurisdiction on a court of the United States which it would not otherwise have. The complaint shall also allege with particularity the efforts, if any, made by the plaintiff to obtain the action the plaintiff desires from the directors or comparable authority and, if necessary, from the shareholders or members, and the reasons for the plaintiff's failure to obtain the action or for not making the effort. The derivative action may not be maintained if it appears that the plaintiff does not fairly and adequately represent the interests of the shareholders or members similarly situated in enforcing the right of the corporation or association. The action shall not be dismissed or compromised without the approval of the court, and notice of the proposed dismissal or compromise shall be given to shareholders or members in such manner as the court directs.

Federal Rule of Civil Procedure 24. Intervention

(a) Intervention of Right. Upon timely application anyone shall be permitted to intervene in an action: (1) when a statute of the United States confers an unconditional right to intervene; or (2) when the applicant

claims an interest relating to the property or transaction which is the subject of the action and the applicant is so situated that the disposition of the action may as a practical matter impair or impede the applicant's ability to protect that interest, unless the applicant's interest is adequately represented by existing parties.

(b) Permissive Intervention. Upon timely application anyone may be permitted to intervene in an action: (1) when a statute of the United States confers a conditional right to intervene; or (2) when an applicant's claim or defense and the main action have a question of law or fact in common. When a party to an action relies for ground of claim or defense upon any statute or executive order administered by a federal or state governmental officer or agency or upon any regulation, order, requirement, or agreement issued or made pursuant to the statute or executive order, the officer or agency upon timely application may be permitted to intervene in the action. In exercising its discretion the court shall consider whether the intervention will unduly delay or prejudice the adjudication of the rights of the original parties.

(c) Procedure. A person desiring to intervene shall serve a motion to intervene upon the parties as provided in Rule 5. The motion shall state the grounds therefor and shall be accompanied by a pleading setting forth the claim or defense for which intervention is sought. The same procedure shall be followed when a statute of the United States gives a right to intervene. When the constitutionality of an act of Congress affecting the public interest is drawn in question in any action in which the United States or an officer, agency, or employee thereof is not a party, the court shall notify the Attorney General of the United States as provided in Title 28, U.S.C. § 2403. When the constitutionality of any statute of a State affecting the public interest is drawn in question in any action in which that State or any agency, officer, or employee thereof is not a party, the court shall notify the

attorney general of the State as provided in Title 28, U.S.C. § 2403. A party challenging the constitutionality of legislation should call the attention of the court to its consequential duty, but failure to do so is not a waiver of any constitutional right otherwise timely asserted.

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No. 97-1732

IN THE

Supreme Court of the United States

OCTOBER TERM, 1998

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM, *et al.*,

Petitioners,

v.

PAUL FELZEN, *et al.*,

Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

BRIEF FOR RESPONDENTS THE DIRECTORS OF ARCHER DANIELS MIDLAND COMPANY

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QUESTION PRESENTED

Whether a nonparty shareholder who appears, in response to notice provided under Federal Rule of Civil Procedure 23.1, to present objections to a proposed dismissal or settlement of a derivative action may appeal an adverse decision even though the shareholder has not been formally made a party to the action.

TABLE OF CONTENTS

PAGE

QUESTION PRESENTED i

TABLE OF AUTHORITIES v

JURISDICTION 1

STATUTE AND RULES INVOLVED 2

STATEMENT OF THE CASE 2

SUMMARY OF ARGUMENT 11

ARGUMENT 12

I. PETITIONERS' DECISION NOT TO SEEK TO JOIN THE ACTION AS REPRESENTATIVE PLAINTIFFS CONTROLS THEIR STATUS AND BARS THEIR AVENUE OF APPEAL 12

A. Derivative Suits, a Creature of the Equity Courts, Proceed Only Within the Procedural Limitations of the Federal Rules 12

1. Only Representative Plaintiffs Who Abide by the Rule May Proceed 14

2. The Derivative Plaintiffs Represent the Shareholders in Seeking To Cause the Corporation To Act 15

B. Shareholders Who Do Not Feel That Their Interests Are Being Represented Must Intervene To Play a Meaningful Role in the Derivative Litigation 18

C. Petitioners Chose Not To Intervene in Order To Advance Their Private Agenda Without the Obligations Imposed Upon Representative Plaintiffs 24

II. NONPARTY SHAREHOLDERS SEEKING TO APPEAL FROM APPROVAL OF A DERIVATIVE SETTLEMENT FALL OUTSIDE THE LIMITED CLASS OF NONPARTIES HISTORICALLY PERMITTED TO APPEAL 32

A. Petitioners Misconstrue the Status of Shareholders in a Derivative Action .. 32

B. The Precedent Cited by Petitioners Does Not Support a Rule That Nonparty Shareholders in a Derivative Action Should Be Permitted To Appeal 34

1. *Johnson, Cohen* and Related Decisions 35

2. *Blossom v. The Milwaukee & Chicago Railroad Co.* and *Williams v. Morgan* 38

3. *United States ex rel. Louisiana v. Judge Boarman* 40

4. Other Cases 42

a. Cases Binding a Nonparty by Name 43

b. Attorneys' Fees 44

c. Nonparties Obligated To Reimburse Defendants 44

C. Rule 23.1 Does Not Embody the Concept of Nonparty Shareholders as "*De Facto* Parties" or "Quasi-Parties" 45

CONCLUSION 48

TABLE OF AUTHORITIES

Cases **Page(s)**

Arizonans for Official English v. Arizona, ___ U.S. ___, 117 S. Ct. 1055 (1997) 23, 24

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Brehm v. Eisner, Docket No. 469, 1998 (Del.) 31

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476 U.S. 54 (1986) 23

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897 F.2d 1499 (9th Cir.),
cert. denied sub nom. Keith v. EEOC, 498 U.S. 815 (1990) 43

Ex parte Cutting,
94 U.S. 14 (1876) 42

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629 F.2d 825 (2d Cir. 1980) 44

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(1st Cir. 1975) 15

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962 F.2d 1203 (6th Cir. 1992) 25

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(9th Cir. 1990) 43

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115 F.R.D. 177 (N.D. Ill. 1987) 16

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104 U.S. 450 (1881) 13

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___ U.S. ___, 118 S. Ct. 1969 (1998) 2

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705 A.2d 238 (Del. Ch. 1997) 17

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325 U.S. 335 (1945) 23

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510 U.S. 27 (1993) 2

Johnson v. Manhattan Ry. Co.,
289 U.S. 479 (1933) 35, 36, 37

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594 A.2d 48 (Del. 1991) 17

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900 F.2d 1363 (9th Cir.),
cert. denied sub nom. Round Table Pizza, Inc. v. Larson,
498 U.S. 1012 (1990) 15

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671 F.2d 779 (3d Cir.), *cert. denied*, 459 U.S. 880 (1982) 15

Marino v. Ortiz,
484 U.S. 301 (1988) 11, 34, 42

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48 F.2d 79 (9th Cir. 1930), *cert. denied*, 283 U.S. 864 (1931) 37

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449 F.2d 506 (6th Cir. 1971) 15

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77 F.2d 888 (2d Cir. 1935) 37

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32 A.D.2d 247, 300 N.Y.S.2d
630 (N.Y. App. Div. 1969) 14

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783 F.2d 829 (9th Cir.), *cert. denied sub nom. DeLusignan v. Gould*, 479 U.S. 818 (1986) 43

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35 F.3d 1056 (6th Cir. 1994) 37

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489 F.2d 579 (5th Cir.), *cert. denied*, 419 U.S. 873 (1974) 15

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648 F.2d 1144 (8th Cir. 1981) 43

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Case No. 97 CH 1440, Circuit Court of Cook County, Illinois, Chancery Division 18, 31

United Airlines, Inc. v. McDonald,
432 U.S. 385 (1977) 21

United Copper Secs. Co. v. Amalgamated Copper Co.,
244 U.S. 261 (1917) 13

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Index No. 106285/95, Supreme Court of the State of New York, New York County, Commercial Division ..... *passim*

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138 F.3d 608 (6th Cir. 1998) 33, 37

Williams v. Morgan,
111 U.S. 684 (1884) 39, 40

Constitution, Statutes, and Rules

U.S. CONST. art. III 23

15 U.S.C. § 16(b)-(H) 46

28 U.S.C. § 1254(1) 1, 2

42 U.S.C. § 9622(d)(2) 47

Equity Rules

Rule 27 ..... 2, 13

Rule 94 ..... 2, 13, 14

Federal Rules of Civil Procedure

Rule 23 ..... *passim*

Rule 23.1 ..... *passim*

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No. 97-1732

IN THE

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Petitioners,

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PAUL FELZEN, *et al.*,

Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

BRIEF FOR RESPONDENTS THE DIRECTORS OF ARCHER DANIELS MIDLAND COMPANY

JURISDICTION

Title 28 U.S.C. § 1254(1), which petitioners invoke for this Court's jurisdiction, Pet. Cert. 1, authorizes review of cases in the courts of appeal by writ of *certiorari* "granted upon the petition of any party to any civil or criminal case." Petitioners describe themselves as "parties in the court of appeals." Pet. Br. ii.

This Court has said that "[o]ne who has been denied the right to intervene in a case in a court of appeals may petition for a writ of *certiorari* to review that

ruling." *Izumi Seimitsu Kogyo Kabushiki Kaisha v. U.S. Philips Corp.*, 510 U.S. 27, 30 (1993); *cf. Hohn v. United States*, ___ U.S. ___, 118 S. Ct. 1969, 1975-76 (1998). Petitioners specifically claimed a right to appeal as nonparties, J.A. 349, and did not seek to intervene in either the district court or the court of appeals. It appears that jurisdiction under § 1254(1) may be lacking.

STATUTE AND RULES INVOLVED

Rules 23, 23.1 and 24 of the Federal Rules of Civil Procedure, 28 U.S.C. § 1254, and former Federal Equity Rules 27 (1912) and 94 (1882) are reproduced as addenda to the brief filed by respondent Archer Daniels Midland Company.

STATEMENT OF THE CASE

The facts which gave rise to this action are not disputed. Certain material matters, however, have been overlooked by petitioners in their brief. These facts should be kept in mind in considering whether to grant objecting shareholders, who do not purport to act for *all* shareholders of the Archer Daniels Midland Company, the right to delay implementation of a settlement of a *corporate* claim to which more than 99% of the corporation's shareholders do not object.

These derivative actions were brought by two separate plaintiffs ("representative plaintiffs") in the name of the Archer Daniels Midland Company ("ADM" or the "Company"). JA 48. Their claims were consolidated in the United States District Court for the Central District of Illinois. The representative plaintiffs sought to assert

claims against the seventeen directors of the Company as of June 27, 1995 ("director defendants") for alleged breaches of their fiduciary duties, for abuse of their control of the Company and for gross mismanagement in failing to prevent ADM employees from violating the law. JA 56.[1] The claims stemmed from the highly publicized investigation of ADM, some of its employees, and a number of its competitors, for alleged price-fixing in the markets for lysine, citric acid and high fructose corn syrup. When the Company pleaded guilty to fixing prices in the lysine and citric acid markets, paying a $100 million fine, the representative plaintiffs amended their claims to assert further breaches of fiduciary duty by the director defendants in their failure to investigate these allegations and to cooperate with the government in pursuing two of the three ADM employees personally indicted (and ultimately convicted) for their role in the lysine scheme. JA 95-105.

The Company and the director defendants moved to dismiss the claims because the representative plaintiffs had failed to make the requisite demand on the Company's board of directors under Rule 23.1 of the Federal Rules of Civil Procedure ("Rules") to pursue these claims, and had failed to allege particularized facts why such a demand would be futile under Delaware law. The Company and the director defendants also asserted that Article Fourteenth of the Company's certificate of

---

[1] Fourteen similar claims were filed by representative plaintiffs and consolidated in the Court of Chancery of New Castle County, Delaware. JA 108-09, 160. ADM is organized and exists under the laws of Delaware. Its principal place of business is in Decatur, Illinois. JA 36. Delaware law governs the conduct of the Company's affairs.

incorporation shielded its directors from liability for their actions as directors. JA 110. The motion to dismiss was granted on April 26, 1996. JA 201. The representative plaintiffs were given leave to amend, which they did. Although discovery is routinely denied plaintiffs while such motions are pending, the representative plaintiffs reviewed over 170 boxes of documents which ADM had placed in a depository, scouring for evidence to support their allegations of board wrongdoing or demand futility. JA 161. Yet, faced with a renewed motion to dismiss on the same grounds, the representative plaintiffs were forced to admit that they had found "no evidence that any director of ADM, other than Michael D. Andreas, was aware of any price fixing activities, or that the ADM Board systematically failed to exercise its oversight responsibilities." JA 205.

The representative plaintiffs then initiated settlement discussions with the Company and the director defendants. After several months of negotiations, the representative plaintiffs agreed that it would be appropriate to settle the derivative suit if the Company (1) agreed to implement specific changes in the way in which the Company governed itself; (2) agreed to reserve the claim which the Company may have against the one director defendant and the other officers indicted for fixing prices, with any such claims to be considered by disinterested directors at final disposition of the criminal claims against that director and those officers;[2] and

[2] All ADM employees except two received immunity from prosecution as a condition of the corporate plea. These two former officers, along with a former government mole, were found guilty of price-fixing on September 17, 1998. The Memo-

(continued...)

(3) agreed to maintain an Audit Committee of non-management directors for a period of at least three years to review the Company's law compliance and to investigate whether the Company was engaged in anti-competitive activities in any market in which it does business. JA 211-12. The director defendants also prevailed upon their insurance carrier to create an $8 million escrow to settle the derivative claims, with the Company to receive the balance of the monies to fund the activities of the Audit Committee after the representative plaintiffs' costs and counsel fees had been paid. JA 196, 210.

By the time the settlement terms were agreed, several significant changes had taken place at the Company. Of the seventeen director defendants, ten had resigned or retired from the board, and an eleventh had retired from the Company. Five new independent

[2] (...continued)

randum of Understanding executed between the Company and the representative plaintiffs committed the decision to pursue corporate claims against the two officers to the Company's board after final disposition of the criminal proceedings, as provided in the indemnification agreements executed pursuant to Article X of the Company's by-laws. This by-law setting the disinterested directors' obligation to consider appropriate claims at final disposition of the government's claims against these individuals was a significant impediment to successful prosecution of any derivative claim: "A decision whether or not a corporation will sue an alleged wrongdoer is no different from any other corporate decision to be made in the collective discretion of the disinterested directors." *Burks v. Lasker*, 441 U.S. 471, 486 (1979) (Stewart, J., concurring).

The Delaware plaintiffs agreed to be bound by the terms of the settlement presented to the district court. Those actions are stayed pending this Court's decision, but will be dismissed upon final dismissal of the consolidated action below. JA 123.

directors had been added to the board. JA 207, 210. The board of directors had shrunk to thirteen, with a clear majority of outside directors. JA 280. The only management member of the board was the Company's new Chief Executive Officer. JA 280. Counsel for the representative plaintiffs recognized that these changes were consistent with their litigation goals, JA 210, but also posed legal impediments to their maintenance of a derivative suit in the face of a newly independent board of directors who were no longer even inferentially dominated by interested defendant directors. JA 214.

During these settlement discussions, the representative plaintiffs consulted with a number of the Company's institutional investors. Months before a settlement was reached, counsel for the representative plaintiffs met with the general counsel of petitioner California Public Employees' Retirement System ("CalPERS"), the Deputy Controller for Pensions of New York City, a representative of the Teamsters Pension Fund, a representative of the Carpenters Pension Fund, and two representatives of *amicus* Council of Institutional Investors ("CII"), to advise them of the negotiations and likely settlement terms. JA 208-09. The representative plaintiffs also engaged experts in the field of corporate governance to analyze the elements of the proposed settlement. JA 209. Similarly, the director defendants surveyed the field of corporate governance. JA 209. Both sides offered affidavits to the district court analyzing the nature of the governance reforms reflected in the proposed settlement.

As reflected in the affidavit submitted to the district court by John C. Coffee, Adolf A. Berle Professor of Law at Columbia University Law School, the governance

provisions developed during the settlement process "represent more or less the 'state of the art' in American corporate governance today." JA 226. Professor Coffee compared the governance provisions in the proposed settlement with the American Law Institute's PRINCIPLES OF CORPORATE GOVERNANCE: ANALYSIS AND RECOMMENDATIONS (1992), the CORPORATE DIRECTORS HANDBOOK prepared by the Business Law Section of the American Bar Association (49 BUS. LAW. 1243 (1994)), CII's Shareholder Bill of Rights, CalPERS' proposed governance guidelines, the guidelines of the National Association of Corporate Directors, and the 1994 General Motors Guidelines on Significant Corporate Governance Issues. JA 225-26. Professor Coffee concluded that the governance provisions of the proposed settlement "do that which can feasibly be done: establish a framework for effective monitoring and facilitate the evolution (which will not necessarily occur overnight) of an active and independent board." JA 231. Similarly, Michael P. Dooley, William S. Potter Professor of Law at the University of Virginia, surveyed the corporate governance structure of other corporations, studied recent changes which other corporations had made in their governance structures, and conducted an exhaustive review of the corporate governance literature. JA 277. Professor Dooley concluded that the proposed settlement terms "will move ADM to the very forefront of American corporations in terms of corporate governance." JA 281. Based upon this advice, the parties reached a decision which provides petitioners' motivation for this appeal: the representative plaintiffs, the Company and the director defendants declined to adopt wholesale CalPERS' governance recommendations.

The district court preliminarily approved the proposed settlement and notice of the settlement was sent to the holders of over 525 million shares of ADM stock. The notice stated that it was being sent "merely to advise you of the pendency and proposed Settlement of the Derivative Claims and of your rights thereunder." JA 135. The notice also advised that "[a]ny current shareholder of ADM may appear at the Settlement Hearing." JA 140. On the day the notice was mailed, CalPERS and CII were aware of the specific terms of the settlement. JA 313. CalPERS, along with petitioner Florida State Board of Administration ("FSBA"), filed objections to the settlement, supported by two affidavits submitted to the district court by CII (an organization of which CalPERS and FSBA are two of the largest members, JA 318). CalPERS and FSBA were but two of the Company's 367 institutional shareholders; none of the other 365 objected. JA 343. The total number of shares objecting to the settlement comprised less than 1% of the outstanding holdings of the Company's shareholders. JA 343. All objections were considered by the district court on July 7, 1997.

CalPERS and FSBA objected to two elements of the proposed settlement: the amount of the settlement escrow to be paid to attorneys; and the governance changes themselves, particularly the definition by which the Company would assess a director's "independence" of management. Petitioners did not object to the principal agreement in the proposed settlement that any claims against the only director against whom the representative plaintiffs had developed evidence would be considered by the Company's board of directors after final disposition of the government's claims against that

director. Petitioners also did not object to the establishment of an Audit Committee composed entirely of non-management directors who had joined the board *after* the events giving rise to the claims. Nor did petitioners object to the mandate of a compliance review and complete antitrust audit of the Company's activities. Instead, petitioners made oblique suggestions of possible collusion in the proposed settlement. JA 305-06. When the district court demanded clarification of their objection, however, petitioners denied that they were claiming impropriety in the way the settlement was reached. JA 338 ("I make no assertion of any impropriety, Your Honor.").

Petitioners also did not comment on the patent weaknesses in the representative plaintiffs' claims under Delaware law arising from plaintiffs' failure to make a demand upon the Company's board of directors to pursue these claims, or from the protections afforded the director defendants by the Company's articles of incorporation. In their original objection, petitioners focused entirely on attorneys' fees and governance principles. They made no objection to the settlement escrow of $8 million, taken from a $10 million insurance policy that contained exclusions potentially applicable to the conduct which the representative plaintiffs had alleged, other than to say that too much money would be going to lawyers.[3]

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[3] The Company and the director defendants left the issue of plaintiffs' attorneys' fees to the district court's discretion. Contrary to petitioners' assertion that the balance of the settlement funds remaining after payment of plaintiffs' counsel would go to even more lawyers, the escrow is committed to the

(continued...)

Petitioners did object to the definition of "independence" to be used in evaluating the Company's non-management directors. Petitioners urged the same definition of independence which they had proposed at the Company's 1996 annual meeting; that proposal failed in a shareholder vote. JA 318-19. Petitioners therefore sought to derail the settlement reached with the representative plaintiffs unless petitioners' definition of independence was adopted as a part of the settlement. The district court confronted this controversy in colloquy, JA 340, with petitioners' counsel:

> THE COURT: They didn't agree with you in summary.
>
> MR. HANSEN: I am sorry.
>
> THE COURT: I say they didn't agree with you.
>
> MR. HANSEN: They didn't negotiate.
>
> THE COURT: With your clients, they didn't agree with your clients.

The district court overruled petitioners' objections and approved the proposed settlement. Petitioners did not thereafter seek to intervene pursuant to Rule 24, or otherwise to appear to represent the interests of the Company's shareholders under Rule 23.1. Within seven days of the district court's order approving the settlement, petitioners filed a notice of appeal to the United States Court of Appeals for the Seventh Circuit. JA 28. The representative plaintiffs moved to dismiss the appeal on the jurisdictional ground that petitioners had never become parties to the action below under Rule 23.1, and should not be allowed to circumvent the provisions of that Rule to delay implementation of a settlement favored by 99% of the Company's shares in order to advance petitioners' own governance agenda. JA 32. The court of appeals agreed and dismissed the appeal on the authority of this Court's decision in *Marino v. Ortiz*, 484 U.S. 301 (1988). JA 33. This Court granted petitioners' request for a writ of *certiorari* on September 29, 1998, restricted to the question whether an objecting nonparty shareholder may appeal the settlement even though the shareholder has not been formally made a party to the action. JA 351.

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[3] (...continued)
Company's Audit Committee "to satisfy its independent review responsibilities as set forth in Exhibit A [to the settlement], and for any training or educational efforts undertaken at the Audit Committee's direction." JA 119.

SUMMARY OF ARGUMENT

Petitioners made a decision not to join the action below as parties and have no right to appeal. Under the rule governing federal derivative actions, shareholders' participation is strictly limited, and only those who meet the requirements of Rule 23.1 may become parties and appeal from the district court's decision. The rule reflects the essential nature of a derivative action, which is not an action brought by shareholders for their own benefit, but one brought by representative shareholders to enforce a right of the corporation. As a result, petitioners must have done more than simply object to settlement of a suit—which is what the rule permits—if they expected to create a right to appeal. That avenue, intervention under Rule 24, was readily available to petitioners. Despite the fact that they have taken advantage of that avenue in other cases, petition-

ers declined to do so in this case, depriving the Seventh Circuit of appellate jurisdiction.

The court of appeals' refusal to permit petitioners to circumvent the rules governing derivative actions is not inconsistent with the precedent, discussed at great length in the briefs of petitioners and the government, which permits nonparties to appeal under certain circumstances. In fact, all of these cases involve nonparties who were directly bound or affected by a court order. Many of them involved nonparties who were effectively named in what may be characterized as process issued by the court. Such cases are distinct from a derivative suit, where only the corporation is directly bound or affected by the court's approval of a settlement. The rules permit a shareholder to receive notice of and be heard on a proposed settlement, but because of the shareholder's distance from the suit, they permit nothing more.

ARGUMENT

I. PETITIONERS' DECISION NOT TO SEEK TO JOIN THE ACTION AS REPRESENTATIVE PLAINTIFFS CONTROLS THEIR STATUS AND BARS THEIR AVENUE OF APPEAL.

A. Derivative Suits, a Creature of the Equity Courts, Proceed Only Within the Procedural Limitations of the Federal Rules.

A derivative suit is a corporate claim which some shareholders, purporting to speak for *all* shareholders, assert for the corporation because the board of directors has failed to make the claim. One or more shareholders are permitted "to step into the corporation's shoes and to seek in its right the restitution he could not demand

on his own." *Cohen v. Beneficial Indus. Loan Corp.*, 337 U.S. 541, 548 (1949). Since corporations are run by their directors, and not by their shareholders, the rules governing derivative suits reflect the basic policy that, "whether or not a corporation shall seek to enforce in the courts a cause of action for damages is, like other business questions, ordinarily a matter of internal management, and is left to the discretion of the directors . . . ." *United Copper Secs. Co. v. Amalgamated Copper Co.*, 244 U.S. 261, 263 (1917). Therefore, there are safeguards built into the rules governing derivative claims which all derivative plaintiffs must follow, to assure that the action is truly to "enforce a right of a corporation . . . the corporation . . . having failed to enforce a right which may properly be asserted by it . . . ." Rule 23.1.[4]

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[4] Procedural limitations on the use of the derivative avenue have always been a part of this Court's rules to assure shareholders a remedy for faithless management while guarding the corporation against abusive shareholders. *See generally Daily Income Fund, Inc. v. Fox*, 464 U.S. 523, 529-34 (1984). In its second opportunity to consider a derivative claim, the Court set rules which survive today in the requirements of Rule 23.1: (1) demand of the board of directors; (2) contemporaneous ownership of the shares; and (3) allegations that the suit was not collusive in order to confer federal jurisdiction. *Hawes v. Oakland*, 104 U.S. 450, 460-61 (1881). These requirements were implemented first in Equity Rule 94, then in Equity Rule 27, and later in Federal Rule of Civil Procedure 23(b). *See* Supplementary Advisory Committee Note to Federal Rule of Civil Procedure 23 (1937).

1. Only Representative Plaintiffs Who Abide by the Rule May Proceed.

The Rule provides that each representative plaintiff must have been "a shareholder . . . at the time of the transaction of which the plaintiff complains." Rule 23.1(1). The Rule also provides that the plaintiff allege with particularity "the efforts, if any, made by the plaintiff to obtain the action the plaintiff desires from the directors . . . ." Rule 23.1. Each plaintiff also must set out with particularity "the reasons for the plaintiff's failure to obtain the action or for not making the effort." *Id.* Finally, the Rule provides that "the derivative action may not be maintained if it appears that the plaintiff does not fairly and adequately represent the interests of the shareholders . . . similarly situated in enforcing the right of the corporation . . . ." *Id.*[5]

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[5] The requirement that plaintiffs fairly and adequately represent the interests of the shareholders of the corporation was adopted as a curb against strike suits by shareholders pursuing their own agendas to the detriment of the corporation and the majority of its shareholders. In the sixty years following implementation of Equity Rule 94, many states confronted abuse of the derivative action by enacting security-for-expense statutes in the hope that "a stockholder motivated by personal gain instead of the welfare of the corporation . . . would be deterred from bringing a spurious action, when the onus of the expense incurred by the corporation in defending it would be ultimately cast on the plaintiff as a consequence of the exposure of the action as meritless." *Roach v. Franchises Int'l, Inc.*, 32 A.D.2d 247, 250, 300 N.Y.S.2d 630, 633 (N.Y. App. Div. 1969). *See* Note, *Security for Expenses in Shareholders' Derivative Suits: Twenty-Three Years' Experience*, 4 COLUM. J.L. & SOC. PROBS. 50, 52 (1968). Neither the federal courts nor the courts of Delaware adopted such statutes, but both added the requirement that a plaintiff prosecuting a derivative action must fairly and adequately represent the interests of the shareholders as a precondition to the action.

2. The Derivative Plaintiffs Represent the Shareholders in Seeking To Cause the Corporation To Act.

The representative plaintiffs and their counsel are subject to attack when they do not represent the interests of the shareholders in their effort to cause the corporation to act. The lower courts have been sensitive to any conflict of interest between the named derivative plaintiff and the other owners of the corporation. *G.A. Enters., Inc. v. Leisure Living Communities, Inc.*, 517 F.2d 24 (1st Cir. 1975); *Nolen v. Shaw-Walker Co.*, 449 F.2d 506 (6th Cir. 1971). If a shareholder has interests which make it impossible for the shareholder to act in the interests of the other shareholders, the named plaintiff is not allowed to serve. *See Larson v. Dumke*, 900 F.2d 1363, 1367 (9th Cir.), *cert. denied sub nom. Round Table Pizza, Inc. v. Larson*, 498 U.S. 1012 (1990). Courts examine any evidence which suggests that the plaintiff will disregard the interests of the other shareholders in prosecuting the action. *See Lewis v. Curtis*, 671 F.2d 779 (3d Cir.), *cert. denied*, 459 U.S. 880 (1982); *Smallwood v. Pearl Brewing Co.*, 489 F.2d 579 (5th Cir.), *cert. denied*, 419 U.S. 873 (1974). Among the factors to which the courts have looked in evaluating the adequacy of a representative plaintiff are economic antagonism between the representative and the other shareholders, the relative magnitude of plaintiff's personal interests as compared to its interest in the derivative action itself, the remedy sought by the plaintiff compared to the benefit which it would confer upon the corporation and the other shareholders, and any vindictiveness which the named plaintiff may have against the defendants. *Larson v. Dumke*, 900 F.2d at 1367 (listing eight factors*); see also Rothenberg v.*

Security Management Co., 667 F.2d 958, 961 (11th Cir. 1982); *Davis v. Comed, Inc.*, 619 F.2d 588, 593-94 (6th Cir. 1980).

Yet derivative actions can be maintained by representative plaintiffs which do not have the support of a majority of the shareholders, provided that their actions meet the requirements of the Rule. *Halsted Video, Inc. v. Guttillo*, 115 F.R.D. 177, 179 (N.D. Ill. 1987).[6] If the

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[6] Adequacy of representation of shareholders in a derivative action is different from the issues that arise in the context of a class action under Rule 23. Rule 23.1 "requires that the shareholder allege that he is enforcing a right of the corporation that it refuses to enforce, a decision typically arrived at through a vote of its shareholders." 7C CHARLES A. WRIGHT, ET AL., FEDERAL PRACTICE AND PROCEDURE § 1833, at 137 (2d ed. 1986). The representative plaintiff speaks for those shareholders who assert that the company failed to act on a corporate right because they collectively seek to compel the corporation to act, regardless of their number. The distinction between Rule 23 and Rule 23.1 sharpens analysis of the adequacy of the representative plaintiffs: in a Rule 23 class action, courts must consider the size of the class in deciding whether to allow the claim to proceed, but that is not considered in a derivative context because:

> it has always been clear that a derivative action can be brought when the number of shareholders is too small to justify a class action. Because the derivative suit is brought to enforce the right of the corporation and the stockholders will benefit only indirectly, it has been thought that dollar amounts or numbers of representatives involved should not be relevant.

Id. at 140-41.

The focus on whether the plaintiffs represent the interests of the shareholders, rather than whether the number of shareholders is large enough to warrant attention, derives from the essential nature of a derivative suit. *See* 7C WRIGHT, ET AL., (continued...)

plaintiffs prevail, the benefit flows to the corporation, thereby conferring an indirect benefit on all shareholders. *See Cohen*, 337 U.S. at 548. Personal claims which a representative plaintiff may assert for itself are not affected by resolution of the derivative claims. *See, e.g., In re Louisiana-Pacific Corp. Derivative Litig.*, 705 A.2d 238, 241 (Del. 1997); 7C CHARLES A. WRIGHT, ET AL., FEDERAL PRACTICE AND PROCEDURE § 1840 at 196-201 (2d ed. 1986). Any representative plaintiff willing to soldier forward against a decision of the board of directors can win the benefit for all shareholders, whether or not those shareholders support the action. Ostensibly to win such benefits for all shareholders, CalPERS had intervened in at least two well-publicized cases before lodging its objection below.[7] For some

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[6] (...continued)

supra, § 1833, at 137. The drafters of Rule 23.1 gave effect to this distinction after "a preliminary analysis" of old Rule 23 "resulted in shearing away and dealing separately with the special situations of derivative actions . . . ." Benjamin Kaplan, *Continuing Work of the Civil Committee: 1966 Amendments of the Federal Rules of Civil Procedure (I)*, 81 HARV. L. REV. 356, 386-87 (1967). As Professor Kaplan put it, derivative actions "do not fit in the groove of class actions . . . they require special provisions regarding preconditions of suit such as demands on the corporation to bring the action." *Id.* at 387 n.118. Thus, the adequacy requirement of Rule 23.1 "are also intended to prevent shareholders from suing in place of the corporation in circumstances where the action would disserve the legitimate interests of the company or its shareholders." *Daily Income Fund, Inc.*, 464 U.S. at 532 n.7.

[7] *See Weiser v. Grace*, Index No. 106285/95, Sup. Ct., N.Y. Cty., N.Y., Commercial Division; *Kahn v. Sullivan*, 594 A.2d 48, 50 (Del. 1991). Petitioner FSBA has intervened and asserted derivative claims in at least one action. *See Board of* (continued...)

reason, however, petitioners chose not to assert the Company's claims below, either as parties plaintiff or as intervenors.

B. Shareholders Who Do Not Feel That Their Interests Are Being Represented Must Intervene To Play a Meaningful Role in the Derivative Litigation.

When there is a complaint about the adequacy of the representative plaintiffs or their counsel in a derivative action, the appropriate vehicle is to intervene under Rule 24. 7C WRIGHT, ET AL., *supra*, § 1839, at 179 (stating that the purpose of the notice provision of Rule 23.1 is to provide shareholders with sufficient information for them to make a [4]rational decision whether they should intervene in the settlement approval procedure.") The Advisory Committee Notes to the 1966 Amendments to Rule 24 anticipate the arguments which petitioners advance as justification for their decision *not* to intervene and reflect the decision of the drafters in favor of intervention.

Acknowledging that there may have been confusion on the point prior to the 1966 amendment, the Advisory Committee noted that, "[a] class member who claims that his 'representative' does not adequately represent him, and is able to establish that proposition with sufficient probability, should not be put to the risk of having a judgment entered in the action which by its

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[7] (...continued)
Administration of Florida v. Mercury Finance Co. intervening in *Thorpe v. Mercury Fin. Co.*, Case No. 97 CH 1440 (Circuit Court of Cook County, Illinois, Chancery Division).

terms extends to him, and be obliged to test the validity of the judgment as applied to his interest by a later collateral attack." For a shareholder under Rule 23.1 asserting a corporate claim, as opposed to a personal claim, there can be no collateral attack for inadequate representation as in a class action—he therefore has the option to enter the action below to press his position on behalf of the corporation. Intervention by shareholders in derivative suits is entirely consistent with the Advisory Committee Note to Rule 24 suggesting that a class member who does not feel adequately represented "should, as a general rule, be entitled to intervene in the action."

The Rule 24 avenue to participation and possible appeal is familiar to petitioners. In a recent case in which CalPERS successfully sought to intervene, CalPERS cited these same principles *in favor* of its intervention. *Weiser v. Grace*, Index No. 106285/95, Supreme Court of the State of New York, New York County, Commercial Division. There, the representative plaintiffs and defendants had reached tentative resolution of derivative claims brought against officers and directors of W.R. Grace & Co., on terms which CalPERS believed to be unacceptable. CalPERS moved to intervene either as of right or by permission, and to designate its counsel as plaintiffs' co-lead counsel in the action, under the New York State equivalent of Federal Rule of Civil Procedure 24. In its supporting brief, CalPERS made the following argument:

> CalPERS is not claiming, nor need it claim to intervene as of right, that present co-lead counsel are incompetent or unqualified. Rather, CalPERS is arguing that in this case, on the

specific facts presented, including the fact that they severely narrowed the scope of a possible settlement prior to examining many crucial documents, present co-lead counsel have not been adequately representing the interests of CalPERS as one of W.R. Grace's largest shareholders, or **may** not do so as the case continues. *** CPLR Rule 1012, which is based on Rule 24 of the Federal Rules of Civil Procedure, was intended to and did broaden and liberalize the process of intervention in New York, and "intervention is to be liberally allowed." [New York citation omitted]. Federal cases are in accord: *Trbovich v. United Mine Workers*, 404 U.S. 528, 538 n.10 (1972) ("burden of making showing of [inadequate representation] should be treated as minimal"); *Sierra Club v. Robertson*, 960 F.2d 83, 85-85 [sic] (8th Cir. 1992) (doubts regarding propriety of intervention should be resolved in favor of allowing it).[8]

Characterizing its grounds for intervention in *Weiser* in terms identical to its expression of dissatisfaction with the settlement below, CalPERS asserted that its "allegations of a grossly inadequate settlement coupled with woefully inadequate discovery easily meet the standard for intervention as of right, even without liberal construction."[9] Relying on New York law which is based substantively upon Rule 24, CalPERS noted

[8] Memorandum of Law of CalPERS in Support of Motion To Intervene and To Add Robinson Firm as Lead Counsel and for Related Relief, March 20, 1996, at 6-7 (emphasis in original).

[9] Reply Memorandum of Law of CalPERS in Support of Motion To Intervene and To Add Robinson Firm as Lead Counsel and for Related Relief, April 11, 1996, at 21.

that, "[w]hen the facts warrant, as they do here, a court may add parties *at any stage of an action*, and intervention may be granted even after final judgment."[10] CalPERS specifically relied upon New York precedent for the proposition that a "motion to intervene made after settlement of an action is not untimely where the intervenor is not actually involved in the controversy until after the settlement is reached."[11] The same principle applies under Rule 24. *United Airlines, Inc. v. McDonald*, 432 U.S. 385 (1977).

Petitioners knew the proper way to be heard on behalf of ADM's shareholders; one of them had intervened in *Weiser* one year earlier, forcefully and with success, to do exactly what petitioners professed to want to do below. In *Weiser*, the representative plaintiffs had opposed the effort to intervene, suggesting that CalPERS wait to lodge its objections to a formal settlement agreement. Replying to that suggestion in *Weiser*, in stark contrast to the position which petitioners take here, CalPERS characterized the very method it has employed in this action as "the least efficient way to protect the Grace shareholders from . . . the 'impending resolution' of their claims."[12]

Filing an appearance and objecting has always been thought of differently—and as something less than intervention with correspondingly lesser rights. *See*

[10] *Id.* (emphasis in original).

[11] *Id.* at 21-22 (citing *Hampton Heights Dev. Corp. v. Board of Water Supply*, 136 Misc.2d 906, 519 N.Y.S.2d 438 (Sup. Ct. 1987)).

[12] *Id.* at 14.

Edward Levi & James Moore, *Federal Intervention: II. The Procedure, Status, and Federal Jurisdictional Requirements,* 47 YALE L.J. 898, 938-39 (1938) ("It must be remembered that the right to be heard is not the same as intervention.") Professor Kaplan, Reporter to the Advisory Committee on Civil Rules, noted that this distinction was preserved in the 1966 Amendments to Rule 23, and therefore suggested that it would be advisable to set out in the notice to the class "the rights which the court proposes to allow 'appearing' members" in contrast to the rights afforded "parties." Benjamin Kaplan, *Continuing Work of the Civil Committee: 1966 Amendments to the Federal Rules of Civil Procedure (1),* 81 HARV. L. REV. 356, 392 n.137 (1967).[13]

Petitioners obviously appreciated this distinction. One of the reasons asserted by CalPERS, and accepted by the New York court in *Weiser*, for seeking intervention as opposed to making an objection was that CalPERS wanted to have a "meaningful role in the case."[14] This "meaningful role" may be played only through intervention, as the drafters of the Federal Rules recognized:

> An intervenor must be sharply distinguished from a mere *amicus curiae* or a person who has been heard but has never intervened. Thus stockholders, who file petitions of intervention which are never acted upon, or bondholders

[13] Professor Kaplan opined that an "appearance" entitled "counsel to receive the papers in the action to enable him to follow the case with a view to deciding, *e.g.* whether he should intervene." Benjamin Kaplan, *Continuing Work of the Civil Committee: 1966 Amendments to the Federal Rules of Civil Procedure (1)*, 81 HARV. L. REV. 356, 392 n.137 (1967).

[14] Memorandum of Law of CalPERS, *supra* note 8, at 10 n.4.

> whose petition for intervention is dismissed, may not appeal from a final order entered later in the proceedings, since they were not parties to the action.

Levi & Moore, *supra,* at 906. Those authors emphasized that "the right to be heard is not the same as intervention" and that "[o]ne who is only given a right to be heard, and has not intervened, has no right of appeal." *Id.* at 938 (citing *In re Trust No. 2988 of the Foreman Tr. & Sav. Bank*, C.C.H. Bankr. Serv. ¶ 4216 (7th Cir. 1936) (bondholder who challenged reorganization plan could not appeal from final decree approving final account of trustee)). Similarly, Professor Kaplan noted that applicants who were *denied* intervention "cannot stop a settlement nor, if dissatisfied with the decree entered after contest, press their contentions on appeal . . . ." Kaplan, *supra,* at 405.[15]

[15] This Court has previously recognized that even intervention does not necessarily confer standing to appeal unless the intervenor himself meets the requirements of Article III of the Constitution. *International Union of Mine, Mill and Smelter Workers, Locals No. 15 v. Eagle-Picher Mining & Smelting Co.*, 325 U.S. 335, 338-39 (1945). Although the Court declined to decide "whether a party seeking to intervene before a District Court must satisfy not only the requirements of Rule 24(a)(2), but also satisfy the requirements of Art. III," in *Diamond v. Charles*, 476 U.S. 54, 69 (1986), it later relied upon *Diamond* for the proposition that "[a]n intervenor cannot step into the shoes of the original party unless the intervenor independently 'fulfills the requirements of Article III.'" *Arizonans for Official English v. Arizona*, ___ U.S. ___, 117 S. Ct. 1055, 1067 (1997) (citation omitted). Petitioners urge a rule that would add to the "anomalous decisions in the Courts of Appeal," *id.*, by allowing appeals to be taken by objectors who meet *neither* the requirements of Rule 24 *nor* Article III,

(continued...)

If petitioners' rule were adopted, shareholders could once again buy their shares after the injury, in derogation of Rule 23.1(1), then object and appeal a case which they could not have brought in the first place. *See Daily Income Fund, Inc. v. Fox*, 464 U.S. 523, 531 n.6 (1984) (requirement of pre-suit ownership "is now generally 'aimed at preventing the federal courts from being used to litigate purchased grievances'") (quoting 7A CHARLES A. WRIGHT, ET AL. FEDERAL PRACTICE AND PROCEDURE § 1828, at 341-42 (1st ed. 1972)). But "[t]he decision to seek review is not to be placed in the hands of concerned bystanders, persons who would seize it as a vehicle for the vindication of value interest." *Arizonans for Official English v. Arizona*, ___ U.S. ___, 117 S. Ct. 1055, 1067 (1997) (internal quotations omitted) (quoting *Diamond v. Charles*, 476 U.S. 54, 62 (1986)). Anyone with the ability and experience demonstrated by petitioners must have made a conscious decision, in the cold light of precedent, not to intervene for a private purpose that does not warrant a departure from the plain meaning of the Rules.

C. Petitioners Chose Not To Intervene in Order To Advance Their Private Agenda Without the Obligations Imposed Upon Representative Plaintiffs.

Petitioners' argument that intervention is too burdensome, and therefore would inhibit the settlement

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[15] (...continued)
nor, for that matter, Rule 23.1. This rule does prevent some shareholders from appealing, but they are shareholders who could not have started the suit in federal court.

process, confuses objection with intervention. Some shareholders will always disagree with a proposed derivative settlement. Only a shareholder who is prepared to argue that disagreement with her position is an abuse of the district court's discretion[16] should be allowed to arrest a resolution which the majority of the shareholders favor. To test the district court's exercise of its discretion against the objection on appeal, the shareholder who makes the majority await resolution of her complaint must satisfy all three requirements of Rule 23.1: ownership at the time of alleged injury; effort to put the question to the board; and adequacy of representation. An objector who is not prepared to plead those elements in a Rule 24 petition should not be allowed to invoke the jurisdiction of an appellate court.

The objection raised by petitioners was *not* the nature of the right which the representative plaintiffs sought to assert—recovery against those found guilty of wrongdoing. Nor was the objection raised by petitioners related to the *corporation's* assertion of that right—an issue which the proposed settlement postpones until the time provided in the indemnification agreements executed with the convicted director. The objection was petitioners' view of corporate governance, with which the Company, the directors and the district court disagreed.

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[16] The standard of review for settlement of a derivative claim is whether the district court abused its discretion in approving the terms of the settlement. *E.g., Granada Invs., Inc. v. DWG Corp.*, 962 F.2d 1203, 1204 (6th Cir. 1992); *see* 7C WRIGHT, ET AL., *supra*, § 3902.1 at 182.

Had petitioners sought to intervene, they would have filed the pleading required by Rule 24(c) "setting forth the claim or defense for which intervention is sought." That pleading would have revealed petitioners' purpose to impose a definition of director "independence" upon the company which its shareholders had defeated only eight months before—a definition which would not command the exercise of the district court's discretion exclusively in petitioners' favor. Had they filed such a pleading, petitioners would have been put to the task of explaining why their definition of "independence" was overwhelmingly better than that followed by the ABA, or the ALI, or the NACD, or TIAA-CREF, or by corporations to which CalPERS had given grades of "A" for corporate governance but which still did not follow the definition petitioners advocated below. These issues would have been awkward for petitioners, who have not otherwise justified their guidelines against the field of governance literature now available.[17]

In essence, petitioners avoided the obligations of Rule 23.1—including the obligation to allege ownership at the time of injury, rather than ownership at the time of settlement—and evaded the requirements of Rule 24 and Article III, to press a unique agenda over the expressed desires of 99% of the Company's shareholders.[18]

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[17] Petitioners do not negotiate the terms of their governance guidelines with corporations. Apparently petitioners believe that, were they to agree with a corporation on terms which differ from their published definitions, it would dilute the definitions.

[18] *Amici* Barclay's Global Investors, N.A., and others, argue that strict enforcement of the Federal Rules would prevent (continued...)

With their special interest laid bare, the procedural dilemma into which petitioners claim to have been forced does not seem so harsh. Petitioners chose their avenue by affirmatively deciding *not* to intervene and should not seek to change the law because they chose poorly.

Perhaps the best example of petitioners' overreaching is their claim to the universality of their principle of director independence. Cleverly mixing their terms, petitioners assert that their definition of "independence" is followed by "nearly 85 percent" of the S&P 500. JA 318. But in reality, nearly 85% of the S&P 500 agree only that a majority of their board members should be independent, not that they should meet the CalPERS definition of independence. The affidavit provided to the district court by Professor Coffee describes the other sources, such as the American Law Institute and the American Bar Association, to which a director might look for guidance on issues of corporate governance. JA 225-26.

The objections made by petitioners below ostensibly were based upon CalPERS' staff recommendations proposed, but not adopted, on June 16, 1997. Adam Bryant, *CalPERS Draws A Blueprint for Its Concept of*

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[18] (...continued)
them from being heard. Yet there is no impediment in the Rules to objection—even to those who did not purchase their stock until after the wrong of which complaint has been made. An objector who does not meet the requirements of Rule 23.1, however, cannot say that disagreement with it would be an abuse of discretion and then test the district court's exercise of its discretion on appeal. Those who cannot appeal are those who could not have brought the action in the first instance.

An Ideal Board, N.Y. TIMES, June 17, 1997, at D1. Those staff recommendations were immediately attacked by members of the CalPERS Board, *see, e.g.*, Paul Schnitt, *PERS Directors Reject Principles Aimed at Boards*, SACRAMENTO BEE, June 17, 1997, at C1; Matthew Greco, *CalPERS Debates Stronger Governance*, INVESTOR RELATIONS BUSINESS, June 30, 1997; and withdrawn to facilitate an "open forum" on the role investors such as CalPERS should play in the governance dialogue. *CalPERS Adopts U.S. Corporate Governance Standards*, BUSINESS WIRE, Apr. 13, 1998. On April 13, 1998, CalPERS issued a revised set of governance guidelines, acknowledging that there is "no current agreement as to what constitutes 'independence.'" CalPERS, *Corporate Governance Core Principles & Guidelines*, Apr. 13, 1998, at 8.[19] In objecting, petitioners simply "didn't agree" with the parties, JA 340, but never suggested that it would be improper to adopt a definition of "independence" different from their own.

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[19] Appendix B-2 to the 1998 CalPERS Core Principles shows the differences between the CalPERS proposal and corollaries in the Investment Company Act of 1940, 15 U.S.C. § 80a; regulations under the Securities Exchange Act of 1934, 17 C.F.R. § 240.16b-3; regulations under Section 162 of the Internal Revenue Code, 28 C.F.R. § 1.162-27; regulations governing the FDIC, 12 C.F.R. part 363, app. A.; the by-laws of the National Association of Securities Dealers, subdivision D, Schedule D, Part II; the New York Stock Exchange Listed Company Manual, § 303.00; as well as the ABA *Directors Handbook*, the ALI *Principles of Corporate Governance*, and the NACD 1996 Blue Ribbon Commission on Director Professionalism upon which Professor Coffee had based his comparison. JA 225-26. CalPERS also acknowledged its differences with the Business Roundtable's 1997 Statement of Corporate Governance, which rejected the CII Core Policies upon which petitioners relied below. *See infra* note 20.

Studies being conducted at the time the district court held the settlement hearing showed that the standards which petitioners urged were far from universal. Of the 861 public companies in the Fortune 1000 in the summer of 1997, only *one*—Texas Instruments—met a wide range of these governance tests. Adam Bryant, *The Search for the Perfect Corporate Board*, N.Y. TIMES, August 3, 1997. John Nash, the President of the National Association of Corporate Directors, and a well-known authority on corporate governance, was forced to suggest in the summer of 1997 that, "[t]he pendulum has swung too far, and CalPERS is starting to overreach." *Id.* Subsequently published guidelines on corporate governance, including those by The Business Roundtable and the world's largest pension fund, TIAA-CREF, rejected the approach urged by petitioners below and instead adopted positions on director independence that are consistent with those approved by the district court.[20] Since petitioners had not previously addressed

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[20] Petitioners expressed dismay that ADM's definitions did not impose an absolute bar on any connection between a director and the Company except the director's fee and personal stock holdings. JA 308-09. Since petitioners lodged their objection in the district court, two significant corporate governance statements have been published, both of which reject petitioners' position and embrace definitions of director independence consistent with that adopted in the proposed settlement. TIAA-CREF defined independence to mean "no present or former employment by the company or any significant financial or personal tie to the company or its management which could interfere with the director's loyalty to shareholders." TIAA-CREF Policy Statement on Corporate Governance (October 1997). The Business Roundtable offered the following observation about director independence:

(continued...)

why their definitions were better than those adopted by other influential organizations—and certainly could not show how it would be an abuse of discretion to disagree with their definition of "independence"—a Rule 24

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[20] (...continued)

> The degree of independence of an outside director may be affected by many factors, including the personal stature of the director and any business relationship of the director with the corporation or any business or personal relationship of the director with management. Directors, or firms in which they have an interest, are sometimes engaged to provide legal, consulting, accounting or other services to the corporation, or a director may have an interest in a customer, supplier or business partner of the corporation, or may at an earlier point in his or her career have been an employee or officer of the company. Depending upon their relationship to the director and to the corporation, such relationships may affect a director's actual or perceived independence. The Business Roundtable believes that, where such relationships exist, boards should be mindful of them and make a judgment about a director's independence based on his or her individual circumstances rather than through the mechanical application of rigid criteria. This would involve consideration of whether the relationships are sufficiently significant as to interfere with the director's exercise of independent judgment.

The Business Roundtable, *The Business Roundtable Statement on Corporate Governance*, Sept. 1997, at 10-11.

These definitions are consistent with those previously adopted by the ABA, ALI and NACD, as described in the affidavits of Professor Coffee, JA 327 ("the prevailing approach today among large public corporations"), and Professor Dooley, JA 280, as well as the definition found in the settlement approved below.

pleading seeking to intervene would not have served petitioners' purpose.[21]

Petitioners chose to object, rather than to intervene, for their own reasons. As objectors, they could criticize the settlement, argue for different terms, or even urge that the matter be litigated. To intervene and appeal, however, petitioners must argue that to disagree with them would be an abuse of discretion. To make that argument on appeal, they must show that they meet the requirements of Rule 23.1, either as plaintiffs or as Rule 24 intervenors. Petitioners sidestepped the pleading which intervention would have required while pursuing an agenda distinct from the welfare of the overwhelming majority of ADM shareholders. Had they followed the course chosen by CalPERS in *Weiser* or FSBA in *Mercury Finance*, they could have pressed corporate rights, rather than their own, as Rule 23.1 requires.

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[21] These differences among institutional investors continue, reinforcing the discretionary nature of governance decisions. For example, TIAA-CREF recently withdrew its shareholder resolution challenging Walt Disney Company's definition of director "independence," Joann S. Lublin, *Major Disney Investor Scraps Proposal Calling for Greater Board Independence*, WALL ST. J., December 4, 1998, while CII continues to press its definiation on Disney in court. *See* Motion by the Council of Institutional Investors for Leave To File an *Amicus Curiae* Brief, *Brehm v. Eisner*, Docket No. 469, 1998 (Del.), filed November 19, 1998. Clearly, there is no agreement, even among institutional investors, on the definition which petitioners insist should have been adopted below.

II. NONPARTY SHAREHOLDERS SEEKING TO APPEAL FROM APPROVAL OF A DERIVATIVE SETTLEMENT FALL OUTSIDE THE LIMITED CLASS OF NONPARTIES HISTORICALLY PERMITTED TO APPEAL.

A. Petitioners Misconstrue the Status of Shareholders in a Derivative Action.

Petitioners and the government cite numerous cases, including much 19th century and early 20th century authority, in an effort to place nonparty shareholders in a derivative suit within that small category of "quasi-parties" or "*de facto* parties" who are sometimes permitted to appeal. Pet. Br. 16-28; G. Br. 5-19. In essence, petitioners claim party status because, as they would have it, shareholders given notice of a settlement pursuant to Rule 23.1 are thereby "summoned to court." Pet. Br. 2; G. Br. 6-7. As petitioners see it, allowing them to appeal from settlement of a derivative suit is appropriate because "the shareholder's rights are being adjudicated in the action." Pet. Br. 11.

The fundamental problem with petitioners' view is a misperception of the nature of a derivative action. As explained in the preceding section, it is not the shareholder's rights that are adjudicated in a derivative action; it is the rights of the corporation. Unlike class members in a class action who constitute a plaintiff class, the shareholders do not constitute the corporation on whose behalf a derivative suit is brought. The corporation is an entirely separate entity owned by the shareholders. Any rights to be adjudicated are those of the corporation.

Petitioners similarly distort the character of the notice provisions in Rule 23.1. The Rule says only that

notice of a proposed "dismissal or compromise shall be given to shareholders . . . in such manner as the court directs." There is no order to appear, and, although the practice in the district courts is to afford objecting shareholders an opportunity to be heard, there is no requirement of a hearing or even mention of a right to object. The provision is, on its face, simply a notice provision; yet petitioners would transform it into a command to appear.

As one court of appeals recently observed when faced with a nonparty class member who argued that a notice of settlement meant he had been "summoned into court" and "compelled to appear," it is "only when the court affirmatively orders a non-named party to appear that the party has standing to appeal. [The class member] pushed his way into court; he was not pulled there." *Wilkenson v. Hercules Engines, Inc.*, 138 F.3d 608, 611 (6th Cir. 1998). Indeed, the terms of the notice of hearing below are far removed from a "summons to appear." The notice states that it "is merely to *advise* you of the pendency and proposed Settlement of the Derivative Claims and of your rights thereunder," JA 135, and that "[a]ny current shareholder of ADM *may* appear at the Settlement Hearing . . . ." JA 140 (emphasis added).[22] Petitioners came to court because they

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[22] Petitioners quote from the Order Preliminarily Approving the Notice rather than the Notice itself, and intentionally excise the discretionary verb "may" from their description of the Notice in order to manufacture the following mandatory tone: "(notice directing '[a]ny shareholder of record of ADM' to 'appear and show cause, if he, she, or it has any [reason] why

(continued...)

wanted to do so, not because they were compelled by a court to do so.

B. The Precedent Cited by Petitioners Does Not Support a Rule That Nonparty Shareholders in a Derivative Action Should Be Permitted To Appeal.

The cases cited by petitioners do not constitute a body of law which would encompass the notion that nonparty shareholders are so affected by settlement of a derivative suit that they should have a right to appeal from its approval. *Cf.* Levi & Moore, *supra*, at 906. On the contrary, all of the cases involve nonparties with genuine, direct interests in the proceedings who were compelled to appear in court to protect a right or to make a claim. Only nonparties who fall within this narrow and readily identifiable category should be (and have been) exempted from the rule of *Marino* and permitted to appeal. A prominent treatise, much cited and quoted by petitioners, adopts a similar view:

> When it is possible to seek intervention, however, there is much to be said for requiring that the process of appeal be regularized by seeking intervention. *Appeal by way of a simple notice*

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[22] (...continued)
the proposed settlement of the derivative claims . . . should or should not be entered thereon')." Compare Pet. Br. 8 with JA 148. Such blatant mischaracterization would seem unnecessary if there were any strength in the position that a Rule 23.1 notice should stand alongside court orders from which nonparties historically may appeal.

> *of appeal should be available only to nonparties directly bound or affected by an order.*
>
> 15A CHARLES A. WRIGHT, ET AL., FEDERAL PRACTICE AND PROCEDURE § 3902.1, at 132 (2d ed. 1986) (emphasis added).

The cases upon which petitioners and their *amici* rely all deal with persons directly bound by resolution of their particular claims. They do not reach judgments binding on corporate entities, whose shareholders are collectively bound by their status as shareholders, concerning claims which belong peculiarly to the corporation.

1. *Johnson*, *Cohen* and Related Decisions.

Both petitioners and the government cite cases from the first half of this century for the proposition that the rights of "*de facto*" or "quasi" parties include the right to appeal. Pet. Br. 21-22; G. Br. 5-8. The only decision of this Court cited is *Johnson v. Manhattan Railway Co.*, 289 U.S. 479 (1933), where this Court, according to petitioner, "concluded that corporate shareholders who received notice of proceedings involving a proposed temporary receivership were '*entitled*' to appear in district court—and to appeal—without taking any other steps." Pet. Br. 21 (emphasis by petitioner). Petitioners' summary of the case is at best misleading because *Johnson* involved much more than mere "notice of proceedings." In fact, the shareholders were haled into court by an order to show cause why a receivership should not be continued during the pendency of litigation. *Johnson*, 289 U.S. at 489, 495. Their situation was quite different from nonparty shareholders in a deriva-

tive suit context who are not compelled to appear at all.[23]

Similarly, in *Cohen v. Young*, 127 F.2d 721 (6th Cir. 1942), the shareholder "appeared . . . in answer to the court's notice to show cause" why a derivative action should not be settled; "he was 'like a defendant who is summoned by process of court and after an adverse ruling has the right to appeal.'" 127 F.2d at 124 (quoting *Pianta v. H.M. Reich Co.*, 77 F.2d 888, 890 (2d Cir. 1935)). The decision in *Cohen* hinged on the court's view that the shareholder had in fact been ordered into court under Rule 23(b), something that does not occur under Rule 23.1. The government therefore has it wrong in suggesting that *Cohen* laid the foundation for modern application of any rules, G. Br. 6, other than rules for those responding to court process.

Petitioners would characterize *Cohen* as a watershed; if so, it yields a brackish trickle feeding only those who have been affirmatively and personally called into court outside the ordinary course. In fact, two recent Sixth Circuit cases viewed *Cohen* in exactly that way and refused to permit nonparty class members (who received the same kind of nonmandatory notice as non-

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[23] The government refers to the observation in James Moore & Edward Levi, *Federal Intervention I. The Right to Intervene and Reorganization*, 45 YALE L.J. 565, 592 (1936), that a "stockholder typically cannot intervene in a lawsuit because litigation decisions are controlled by directors and officers of the corporation," G. Br. 7, to support its reading of *Johnson*. In fact, Moore & Levi were talking about the prohibition against intervention by a shareholder into an action being prosecuted or defended by a corporation, not intervention in a derivative suit.

party shareholders in a derivative suit) to appeal from class settlements. In *Shults v. Champion International Corp.*, 35 F.3d 1056 (6th Cir. 1994), the court distinguished *Cohen* as a case where "an unnamed member of a derivative suit who has not been allowed to intervene may nonetheless have standing to appeal if the district court has haled him into court." 35 F.3d at 1060. The court then concluded that "for a non-named class member to have standing to appeal, there must be more than a mere requirement of notice . . . ." *Id.* In *Wilkenson*, the court again noted that the appellant in *Cohen* "had received an order to show cause . . . [and] had no choice but to participate in the proceedings." 138 F.3d at 611. The *Wilkenson* court then rejected the nonparty class member's argument that he similarly had been "summoned" into court: "[i]t is only when the court affirmatively orders a non-named party to appear that the party has standing to appeal." *Id.*

Other cases cited by petitioners and the government in discussing *Johnson* and *Cohen* also involve nonparties who in one way or another received mandatory direction to appear in court. *See Pianta v. H.M. Reich*, 77 F.2d 888 (appeal by nonparty creditor who appeared in response to an order to show cause); *Christian v. R. Hoe & Co.*, 63 F.2d 218 (2d Cir. 1933) (appeal by shareholder and creditor who appeared in response to an order to show cause); *Mitchell v. Lay*, 48 F.2d 79 (9th Cir. 1930) (appealing lower court's injunction, specifically naming the appellant, forbidding him to proceed with certain litigation); *Blake v. District Court*, 59 F.2d 78 (9th Cir. 1932) (appeal dismissed for failure to exhaust remedies below). They do not provide a fair analogy to a shareholder who receives notice of settlement of a

derivative suit to which he may object under Rule 23.1.[24]

2. *Blossom v. The Milwaukee & Chicago Railroad Co.* and *Williams v. Morgan.*

The government places great emphasis on this Court's decision in *Blossom v. The Milwaukee & Chicago Railroad Co.*, 68 U.S. (1 Wall.) 655 (1863), citing it as a prime example of a case where a "quasi-party" is permitted to appeal. G. Br. 9-11, 17. It may be that, but it is also an example of a case where the nonparty, unlike a nonparty shareholder considering whether to settle the corporation's claims in a derivative suit, was directly bound by a court's order.

In *Blossom*, the court foreclosed a mortgage and ordered a sale of the mortgaged property. 68 U.S. at 655. Blossom, a nonparty, made a bid for the property when it was offered for sale, but the sale was then suspended. *Id.* The lower court refused Blossom's petition to have the sale completed, raising the issue of his right to appeal. *Id.* This Court noted that Blossom never could have appealed from the original decree but that, by way of his bid at the foreclosure sale, he fell into a category of "quasi-parties" who "become connected with the case, in the course of the subsequent proceedings, in such a manner as to subject them to the

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[24] The government's reliance on William Haudek, *The Settlement and Dismissal of Stockholders' Actions—Part II: The Settlement*, 22 Sw. L.J. 765, 792 (1968), is misplaced because the author relies only on *Cohen v. Young* and two cases citing to it.

jurisdiction of the court, and render them liable to its orders . . . ." *Id.* at 656. Other persons falling within this category are "[s]ureties, signing appeal bonds, stay bonds, and receipters under writs of attachment" as well as nonparty creditors with an interest in "a fund to be distributed to parties . . . ." *Id.* In other words, the quasi-parties treated in *Blossom* are persons with a direct financial interest in a proceeding.

Nonparty shareholders in a derivative suit do not hold that direct financial interest; their stake is indirect as owners of the entity which itself may have a financial interest. Nor does the notice to shareholders of a settlement under Rule 23.1 "subject them to the jurisdiction of the court" as did Blossom's bid at the court-ordered foreclosure sale. Indeed, this Court found it equitable that Blossom should be able to make his claim because a bidder at a foreclosure sale also "can be compelled to perform his agreement specifically." *Blossom*, 68 U.S. at 656. A nonparty shareholder, of course, subjects himself to no such consequence of jurisdiction. *Blossom*, therefore, is inapposite.

The government cites *Williams v. Morgan*, 111 U.S. 684 (1884), which followed *Blossom*, but only because *Williams* also involved parties with a direct financial interest in a case. When a railroad was sold after a mortgage foreclosure, nonparty bondholders became "virtually the purchasers" of the railroad and thus had a direct interest in the amount of a trustee's compensation. *Id.* at 697. As this Court put it, "it was a matter of great moment to the purchasers, for every dollar allowed to the trustees was so much less for them." *Id.* This Court also noted that such nonparties are "allowed to intervene" and referred to "their right or claim." *Id.*

at 699. The contrast with nonparty shareholders is apparent.

The government cites to several other cases upon which the *Williams* court relied. G. Br. 10-11 n.4. Each of these cases, however, involved a purchaser at a foreclosure sale, a receiver ordered to pay a sum of money, or other nonparty with the same kind of direct financial stake as the bondholders in *Williams*. Early chancery cases cited by petitioners are similar in nature. Pet. Br. 19-20. None deal with the rights of owners of an entity which has its own legal existence, its own management, its own counsel and its own set of rights distinct from those of its owners.

3. *United States ex rel. Louisiana v. Judge Boarman*

Petitioners point to *United States ex rel. Louisiana v. Judge Boarman*, 244 U.S. 397 (1917), the "lone case cited in the pertinent passage of *Marino*," as establishing that "part[ies] *and priv[ies] to the record*" may appeal an adverse decision. Pet. Br. 24 (emphasis by petitioners). According to petitioners, "nonparty shareholders are at least 'privy to the record' in derivative suits," although they neither cite authority for that proposition, nor offer any definition of the term.

The emptiness of petitioners' position—and indeed the general confusion engendered by trying to place nonparty shareholders in the class of nonparties historically permitted to appeal—is reflected in the government's brief. These cases, permitting appeals only by parties or privies, actually state a general rule to which the "quasi-party" cases form a narrow exception. After

reviewing the "quasi-party" cases to support the idea that nonparty shareholders should be allowed to appeal, the government states:

> During the same era in which the Court was developing the narrow right of quasi parties to appeal in limited circumstances, it was also considering numerous cases involving the "well settled maxim of the law, that 'no person can bring a writ of error to reverse a judgment who is not a party or privy to the record.'" *Bayard v. Lombard*, 50 U.S. (9 How.) 529, 551 (1850). Rather than calling into question the general principle that only a party or a privy to the record may appeal, the doctrine of quasi parties complemented – indeed exemplified – that rule. In more recent years, the Court has invoked the general principle that only parties may appeal without mentioning (and, presumably, without intending to cast doubt on) its quasi party cases.

G. Br. 11-12 (footnote omitted).

In other words, the government turns to the quasi-party concept because it concedes that under the strict "parties and privies" rule a nonparty shareholder would not be permitted to appeal—the exact opposite of petitioners' view. Such a fundamental conflict is typical where the applicable precedent, when viewed as a whole, does not support a given position. Its proponents therefore must resort to contriving a regime of *stare decisis* that simply does not exist.

The government's exposition of the "parties and privies only" cases is also quite instructive concerning the kinds of cases where this Court historically has refused to permit nonparty appeals—cases that are

much more closely related to the nonparty shareholder situation involved here. G. Br. 11-12 n.6. For example, in *Ex parte Cutting*, 94 U.S. 14 (1876), this Court refused to hear an appeal by shareholders who sought to defend a mortgage foreclosure involving their corporation. This Court, in language that rings true through to the modern derivative suit context, stated:

> Neither can these petitioners appeal as stockholders. Only parties, or those who represent them, can appeal. The stockholders do not represent the corporation, but for some purposes the corporation represents them. They are sometimes admitted as parties to a suit, for the purpose of protecting their own interests in the corporation against unfounded and illegal claims against it, but this "remedy is an extreme one, and should be admitted by the court with hesitation and caution."

Id. at 19 (quoting *Bronson v. LaCross and Milwaukee R.R. Co.*, 69 U.S. (2 Wall.) 283, 302-03 (1864)).

4. Other Cases.

Petitioners view the Seventh Circuit's application of *Marino* as portending great upheaval in "an enormous body of settled law." Pet. Br. 25. Petitioners then cite to dozens of cases where nonparties have been permitted to appeal in "a wide range of circumstances." Pet. Br. 25. None of these cases, however, is threatened by the Seventh Circuit's decision; in fact, the nonparties in these three categories of cases were the subject of court process, *i.e.*, the courts had issued orders directed to the nonparties. The cases are thus consistent with the older "quasi-party" cases and distinct from a derivative

case where nonparty shareholders have no such direct involvement. Neither together nor individually do they mandate the result petitioners seek.

a. Cases Binding a Nonparty by Name.

Petitioners themselves characterize these cases in a way that makes them clearly distinguishable from derivative suits, *i.e.*, "nonparty appeals from judgments that bind the nonparty by name." Pet. Br. 25. Nonparty shareholders, of course, are not bound by name in any judgment of a district court. The cases cited by petitioners mostly involve injunctions directed to a specific party. Where a nonparty is bound by an injunction, it may appeal its entry. *Thompson v. Freeman*, 648 F.2d 1144, 1148 n.5 (8th Cir. 1981) (citing *Zenith Radio Corp. v. Hazeltine Research, Inc.*, 395 U.S. 100, 110 (1969)). *See also* 15A WRIGHT, ET AL., *supra*, § 3902.1, at 122 & n.35. Others are far removed from the context here. *See, e.g., EEOC v. Pan Am. World Airways, Inc.*, 897 F.2d 1499, 1504 (9th Cir.) (nonparty in age discrimination class action has "personal stake in outcome" and stood "to recover a substantial amount"), *cert. denied sub nom. Keith v. EEOC*, 498 U.S. 815 (1990); *Hal Roach Studios, Inc. v. Richard Feiner and Co.*, 896 F.2d 1542 (9th Cir. 1990) (judgment actually entered against nonparty by name); *SEC v. Wencke*, 783 F.2d 829, 834 (9th Cir. 1986) (a "receiver has haled the nonparty into the proceeding against his will").

Another category identified by petitioners is "nonparty witnesses held in contempt for refusing discovery to appeal on claims of privilege, lack of personal jurisdiction, and other matters." Pet. Br. 25-26. This category, however, is really a subcategory of persons specifically

named in process issued by the court. They all appear because they are compelled to do so; for if they do not, no one else will speak for them. For example, a person summoned to court to show cause why he should not be held in contempt of that court stands in a place far different than a shareholder who receives notice that a corporation in which he owns stock has proposed to settle a derivative claim with plaintiffs who have a duty to speak for him in asserting the corporation's rights.

b. Attorneys' Fees.

Petitioners cite to another group of cases where courts "allow attorneys and expert witnesses to appeal district court denials of fees." Pet. Br. 26. Again, such cases personally address a nonparty and his financial interest. While shareholders certainly have a financial stake in the fate of corporations whose stock they own, any financial recovery in a derivative case goes *to the corporation*, not to the shareholder.

c. Nonparties Obligated To Reimburse Defendants.

Finally, petitioners point to cases where courts permit appeals by nonparties who are "obligated to reimburse the defendant for amounts paid under the trial court's judgment." Pet. Br. 26. One cited example is *Fields v. Blum*, 629 F.2d 825 (2d Cir. 1980), where the court permitted the state to appeal from an order enjoining a reduction in welfare benefits because the state was legally required to reimburse the city for the payments and controlled both the activities complained of and the conduct of the local officials. Pet. Br. 26 n.25. As the

government points out, however, nonparty shareholders are quite different from units of government bound to make public payments. Shareholders are liable only to the extent of their investment—which should not be diminished in a derivative suit—and have no direct obligation to make payments to corporate creditors.

C. Rule 23.1 Does Not Embody the Concept of Nonparty Shareholders as "*De Facto* Parties" or "Quasi-Parties."

Petitioners and the government argue that Rule 23.1, because it was based on "existing law," somehow embodies the principle that nonparty shareholders are entitled to appeal from settlement of a derivative suit. Pet. Br. 18; G. Br. 12-19. This argument suffers from petitioners' misperception of the "existing law" defining the kind of nonparties who have been permitted to appeal. As described in the preceding section, that body of law permits a nonparty to appeal where it is directly bound or affected by a court's action. Rule 23.1 does not contemplate, and does not in practice have, that sort of binding effect on nonparty shareholders who are bound only by the limitations placed upon their corporation. Nonparty shareholders simply are not in the class of persons who, as discussed above, historically have been permitted to appeal a judgment to which they were not parties.

Petitioners go to great lengths to distinguish the status of a shareholder in a derivative suit from that of a shareholder in other suits brought by or on behalf of the corporation. These efforts fail because the argument boils down to the assertion that shareholders should be permitted to appeal because "the shareholders necessar-

ily benefit from whatever recovery the corporation may realize on its claims," G. Br. 12-13, and "the shareholder's rights are being adjudicated in the action." Pet. Br. 11. If such a simplistic test were applied, of course, any shareholder could ignore corporate management, corporate identity and the corporate board to appeal from the final judgment in any action involving the corporation, after trial or otherwise. As the court of appeals observed below concerning *Bell Atl. Corp. v. Bolger*, 2 F.3d 1304 (3d Cir. 1993):

> The third circuit conceived of the question as whether the shareholder has standing, which is misleading. Standing means injury in fact, and a reduction in the market price of one's stock is injury. Parties are a subset of injured persons. Equating injury with party status is exactly the approach disapproved by *Marino*.

134 F.3d at 876.[25]

The government also seeks to distinguish the procedure under Rule 23.1 from provisions in laws such as the Antitrust Penalties and Procedure Act, 15 U.S.C.

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[25] The government, at least, seems to comprehend that granting petitioners what they seek could open the doors to all varieties of shareholder appeals. The government cautions that "recognition of quasi party status . . . should be sparing indeed." G. Br. 15-18. The government suggests allowing an appeal only on the issue to which objection is made; but if the issue is the settlement of the entire claim, then *everything in the case could be appealed.* This plea for a tiny crack in the door for shareholders in a derivative suit neither provides reassurance nor, more importantly, addresses the reality of a shareholder's status pressing a *corporate* claim in a derivative suit. Worse yet, if that door opens under Rule 23.1, the door will swing wide under Rule 23.

§ 16(b)-(H), and the Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA"), 42 U.S.C. § 9622(d)(2), where members of the public are given notice and an opportunity to be heard before entry of a settlement engineered by the government, but have no right to stop the settlement or to take an appeal. The analogy to a government action in the public interest only helps to define the status of a shareholder in a derivative suit by describing another area of the law in which nonparties may appear and object, but must take some additional action if they wish to force appellate review.

In a CERCLA settlement, for example, members of the public are clearly affected—sometimes physically—by the extent to which a contaminated site in their community is remediated. Like nonparty shareholders, they have an interest which the law recognizes by permitting them an opportunity to be heard on a settlement. Yet, like nonparty shareholders, they do not become subject to the jurisdiction of the agency or the courts so as to qualify as "quasi-parties," and thus they have no right to appeal. The statute and regulations circumscribe the rights of the public under CERCLA just as Rule 23.1 delineates the rights of shareholders. The government's argument proves only that there are other areas where notice to those affected by a settlement, and even an opportunity to be heard on the merits of the settlement, does not transform into a "summons to appear" giving rise to a right to appeal.

The exceptions carved for nonparty appeals are rare and limited. The confusion reflected in the contradictions between petitioners' analysis of these cases and that suggested by the government does not compel fur-

ther exceptions. Entities who wish to take an active role in the prosecution of a case have the avenue of intervention provided by Rule 24. It is a fairly easy avenue for shareholders to travel in a derivative suit; they need not try to fit themselves into narrow exceptions. The actions of these petitioners below certainly do not warrant creating new exceptions to the Federal Rules.

CONCLUSION

For the reasons stated, the director defendants respectfully request that this Court affirm the judgment of the United States Court of Appeals for the Seventh Circuit.

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Supreme Court of the United States

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California Public Employees' Retirement System and Florida State Board of Administration,

Petitioners,

v.

Paul Felzen, et al.,

Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

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QUESTION PRESENTED

Whether a nonparty shareholder who appears, in response to notice provided under Federal Rule of Civil Procedure 23.1, to present objections to a proposed dismissal or settlement of a derivative action, may appeal an adverse decision even though the shareholder has not been formally made a party to the action.

TABLE OF CONTENTS

PAGE

QUESTION PRESENTED i

TABLE OF AUTHORITIES iii

JURISDICTION 1

STATEMENT OF THE CASE 1

SUMMARY OF ARGUMENT 8

ARGUMENT 13

I. Only Parties Can Appeal and Objectors Are Not Parties 13

A. Rule 23.1 15

B. Ancillary or Non Caption Parties 17

C. State Law 21

II. Intervention Is an Important Requirement 22

A. Intervention Serves a Meaningful Function 22

B. An Intervention Requirement Does Not Promote Collusive Settlements or Impose Undue Burdens 25

CONCLUSION 27

TABLE OF AUTHORITIES

Cases PAGE

Amchem Prods. Inc. v. Windsor, 117 S. Ct. 2231 (1997) 25

Blake v. District Court, 59 F.2d 78 (9th Cir. 1932) 20

Blossom v. The Milwaukee Railroad, 68 U.S. 655 (1863) 18

In re Brand Name Prescription Drugs Antitrust Litigation, 115 F.3d 456 (7th Cir. 1997) 1, 2, 9

Burks v. Lasker, 441 U.S. 471 (1978) 15

Chase National Bank v. City of Norwalk, 291 U.S. 431 (1934) 16

Christian v. R. Hoe, 63 F.2d 218 (2d Cir. 1933) 19

Cohen v. Beneficial Indus. Loan Corp., 337 U.S. 541 (1949) 24

Cohen v. Young, 127 F.3d 721 (6th Cir. 1942) 16

Daily Income Fund, Inc. v. Fox, 464 U.S. 523 (1984) 15, 22

Grant v. United States, 227 U.S. 74 (1913) 17

Hanna v. Plummer, 380 U.S. 460 (1965) 22

Holden v. Burlington Northern, Inc.,
665 F. Supp. 1398 (D. Minn. 1987) 23

Johnson v. Manhattan Railway Co.,
289 U.S. 479 (1933) 19, 20

Kamen v. Kemper Fin. Servs., Inc.,
500 U.S. 90 (1991) 12, 15, 19

Kingsport Press, Inc. v. Brief English Systems, Inc., 54 F.2d 497
(2d Cir. 1931) 19

Kneeland v. American Loan & Trust Co.,
136 U.S. 89 (1890) 18

Lexecon, Inc. v. Milberg Weiss Bershad Hynes & Lerach, 118 S. Ct. 956 (1998) 20

Marino v. Ortiz, 484 U.S. 301 (1988) ..... *passim*

Martin v. Wilks, 490 U.S. 755 (1989) 11, 16, 25

Matsushita Elec. Indus. Co. v. Epstein,
516 U.S. 367 (1996) 21

Mitchell v. Lay,
48 F.2d 79 (9th Cir. 1931) 19

Ross v. Bernhard, 396 U.S. 531 (1970) 12, 24

Phillips Petroleum Co. v. Shutts,
472 U.S. 797 (1985) 11, 13, 16, 26

Sheldon v. Sill, 49 U.S. 441 (1850) 22

Steel Co. v. Citizens for a Better Environment,
118 S. Ct. 1003 (1998) 20

United States v. Dion, 476 U.S. 734 (1986) 21

United States v. Nixon, 418 U.S. 683 (1974) 18

Walker v. Armco Steel Co.,
446 U.S. 740 (1980) 22

West v. Randall,
29 F. Cas. 718 (C.C. D.R.I. 1820) 10

Statutes and Rules

28 U.S.C. §1254 ..... 1, 9, 14, 17, 25

28 U.S.C. §1291 ..... 17, 20

28 U.S.C. §1651 20

28 U.S.C. §2072 ..... 21, 25

Federal Rules of Appellate Procedure:

Rule 3(c) ..... *passim*

Federal Rules of Civil Procedure:

Rule 4 ..... 11, 16

Rule 17 22

Rule 19 16

Rule 23 . . . . . 11, 18

Rule 23.1 . . . . . *passim*

Rule 24 . . . . . 15, 24

Rules of the Supreme Court
of the United States:

Rule 12 . . . . . 9, 11, 14, 17

Rule 14 . . . . . 9, 11, 12, 14, 17, 21

Miscellaneous

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The Plaintiff's Attorney's Role in Class Action and Derivative Litigation: Economic Analysis and Recommendations for Reform, 58 U.CHI.L.REV. 1 (1991) 23

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75 TEX.L.REV. 571 (1997) 23

JURISDICTION

The Court of Appeals entered its judgment on January 21, 1998. The petition for a writ of certiorari, filed on April 21, 1998, was granted on September 29, 1998. Petitioners invoke the jurisdiction of this Court under 28 U.S.C. § 1254(1).

STATEMENT OF THE CASE

The facts relevant to this petition are simply stated. Respondents, shareholders in Archer Daniels Midland Company ("ADM"), brought this derivative suit in the United States District Court in Illinois, alleging that ADM's directors had violated duties owed to the corporation. A settlement was reached, and pursuant to Fed.R.Civ.P. 23.1, notice of the proposed settlement was given to all the shareholders. Petitioners filed written objections to the settlement and appeared at the settlement approval hearing in opposition to the proposed settlement. At the conclusion of the hearing, the district court rejected their objections, approved the settlement and entered judgment.

Petitioners never sought to intervene in the district court. One week after the district court hearing, however, they filed a notice of appeal to the Court of Appeals for the Seventh Circuit as objectors "entitled to appeal." App. 348-49. Respondents moved to dismiss the appeal in light of Seventh Circuit precedent squarely holding that nonparty class members who do not seek to intervene to become parties may not appeal from district court orders. *In re Brand Name Prescription Drugs Antitrust Litigation*, 115 F.3d 456 (7th Cir. 1997) (Posner, C. J.). The *Brand Name Drugs* decision relied

on this Court's holding in *Marino v. Ortiz*, 484 U.S. 301, 304 (1988), and made clear that *Marino* barred objectors who were not name plaintiffs in representative actions from appealing district court orders. *Brand Name Prescription Drugs*, 115 F.3d at 457. In this case, the Court of Appeals (Posner, C. J., and Flaum and Easterbrook, JJ.) dismissed petitioners' appeal, holding that petitioners as nonparty objectors were not entitled to appeal. The panel's opinion was circulated to the judges of the Seventh Circuit, and no judge favored hearing the case *en banc*. Petitioners sought certiorari from this Court, which the Court granted on the limited issue whether Rule 23.1 objectors who do not intervene can nonetheless appeal.

Despite the apparent simplicity of these facts and the straightforward nature of the legal issue raised by this Court's grant, petitioners' brief is laced with personal attacks upon the conduct of plaintiffs and their counsel. This attack is entirely irrelevant to the issue upon which the writ issued. Petitioners understand that full well. Apparently, they hope that by casting aspersion on plaintiffs' counsel's conduct, this Court will somehow forgive petitioners' failure to seek to intervene. Perhaps we need say no more on this score. But we are unwilling to have the Court proceed on the basis of doubts about plaintiffs' counsel's conduct. The record in this case, including affidavits and the district court's findings, makes clear that petitioners' charges are unwarranted.

Paul Felzen and Sandra Esner are individual shareholders of ADM. They brought this derivative action in the United States District Court for the Northern District of Illinois in July 1995 on behalf of ADM and its

shareholders against 17 ADM directors after the federal government's investigation of illegal price-fixing at ADM was disclosed. Plaintiffs were concerned that the ADM board, long criticized as being dominated by Chairman Dwayne Andreas, whose son was being investigated for price-fixing, would not respond appropriately to the criminal investigation. The case was subsequently transferred to the United States District Court for the Central District of Illinois. Other individual shareholders brought similar derivative actions in Delaware State Court.

Petitioners are two ADM shareholders who own less than one percent of the Company's common stock. Although aware of this litigation and apprised of settlement discussions months before the case was settled, petitioners did not seek to participate in the litigation or make their objections to the proposed settlement known to plaintiffs' counsel until after the parties to the derivative actions had entered into a settlement agreement.

Plaintiffs' counsel prosecuted this lawsuit for nearly two years during which time they reviewed all the documents ADM produced for various civil antitrust litigations, filed amended and supplemented pleadings and briefed successive motions to dismiss and discovery motions. The motions were set for hearing when the parties agreed to discuss settlement. Plaintiffs' counsel agreed to discuss settlement not only because of the risks of this litigation and derivative litigation in general but, more importantly, because they and ADM shareholders believed that the ~~real~~ long term value to ADM would come through corporate governance reforms

that could be obtained only through settlement, but not through litigation. The primary interest of ADM shareholders, including large institutional shareholders, was to make ADM's board more independent and less subject to management control.[1]

In late 1996 and early 1997, plaintiffs' counsel met with and spoke by telephone to large institutional investors, including petitioner CalPERS, amicus, the Council of Institutional Investors ("CII"), the Carpenters Pension Fund, the Teamsters Pension Fund, and an official responsible for New York City's pension fund investments, to solicit their views and input with respect to the litigation and settlement negotiations. CII declined to become involved because a legal action was "politically sensitive," and CII members did not always agree on solutions or with "shareholder activism" in general. App. 329.

Plaintiffs' counsel met with CalPERS' general counsel in San Francisco in February 1997 to discuss the various corporate governance measures that ADM was willing to implement as part of the settlement of the action. Additionally, plaintiffs' counsel specifically advised that ADM was unwilling to adopt all of the provisions of the CII definition of independence as part of a settlement of this case. CalPERS' counsel commented that a somewhat weaker definition of "independence" was "okay" because the CII definition was intended to

[1] Shareholder proposals requiring a majority of independent board members and confidential voting were defeated at ADM's annual meeting of shareholders in 1996, but had each received more than 40% of the votes at ADM's annual meeting.

establish a starting point for negotiations. She then commended plaintiffs' counsel for informing institutional investors of their settlement negotiations and said she would speak to FSBA. App. 330-31. At no time before, during, or after this February 1997 meeting did CalPERS (or FSBA) offer any suggestions or communicate to plaintiffs' counsel any dissatisfaction with the terms of the settlement plaintiffs were negotiating, until one month after the settlement was publicly announced and a few days before CalPERS and FSBA filed their written objections to the settlement in July 1997.[2]

Petitioners acknowledge that a settlement that promotes board independence can provide "significant value" to ADM and its shareholders. App. 321. They attack the settlement, however, because it permits board members who have non-material relationships to ADM to be classified as independent; it incorporates the reforms ADM's Corporate Governance Committee had recommended; it provides for allegedly excessive attorneys' fees in light of the benefits conferred; and because they believe—incorrectly—that all claims are to be released.

The settlement is the result of five months of negotiations among counsel for plaintiffs, the defendant directors and ADM. The settlement is also the result of

[2] Plaintiffs' counsel called CalPERS' general counsel after the settlement agreement was signed. No one from CalPERS returned the call. However, shortly after the district court preliminarily approved the settlement, the CII resurfaced and demanded to know why the settlement did not adopt verbatim CII's definition of an independent director. App. 331-32.

separate negotiations among counsel for the plaintiffs in the Delaware State Court action and defendants which led to certain additions and modifications to the settlement. The settlement incorporates ADM's Corporate Governance Committee's recommendations, which had been approved but not implemented, and further imposes new requirements on ADM—to amend its bylaws to reflect the changes in board requirements and to change the composition and role of key board committees. App. 119, 128-133. The reforms over all have been described by Columbia University Law School Professor John C. Coffee, Jr., with whom plaintiffs' counsel consulted during settlement negotiations, as "more or less the state of the art in American corporate governance" and "significant steps to facilitate board independence and to end the apparent managerial domination of the ADM board." App. 226, 229. Professor Coffee also noted that CII's definition of an "independent" director did not reflect "the prevailing view" and had not been adopted by many public corporations with model corporate governance standards. App. 327.[3]

The settlement requires the director defendants to pay $8 million from their $10 million insurance coverage to the corporation, more than half of which is to be used to pay the cost of implementing the settlement's reforms, including education, training and legal compliance. App. 118, 128-33.[4] Moreover, the newly constituted Audit Committee has been delegated new responsibilities for legal compliance oversight which, according to Professor Coffee, are "of special value" to ADM. App. 226. ADM does not release all claims, but rather retains all claims that it may have against Michael D. Andreas, Terrance Wilson and Mark Whitacre, the only three ADM officials whom the government prosecuted for price-fixing. App. 117-18.[5] Thus the fee award reflects the value placed on the overall settlement, including corporate governance reforms. Petitioners do not disagree that such reforms have value, but disagree with the valuation in this case.[6]

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[3] Despite their position at the settlement approval hearing, petitioners did not resubmit their proposal for defining director independence to a vote of the ADM shareholders.

[4] Petitioners' suggestion (Br. 6 n.7) that plaintiffs' counsel may have a conflict because the Audit Committee could engage them as "outside independent counsel" is preposterous.

[5] Plaintiffs' counsel did not meet with the insurance carrier. The defendants' counsel, however, did meet with the carrier to discuss, among other things, respondents' insistence that claims against Michael Andreas not be released. If ADM fails to take appropriate action to pursue any claims it has against Andreas, Wilson or Whitacre, a shareholder, including CalPERS or FSBA, may bring a derivative action against ADM's Board at the time.

[6] Plaintiffs' financial expert, R. Alan Miller, valued the settlement at $158 million. App. 249. The fee is a small percentage of this number. The fee, less expenses, represented a multiplier of approximately 1.3 of the then lodestar of the Delaware and Illinois plaintiffs. App. 169, 219. Like CalPERS, the Delaware plaintiffs' attorneys requested a fee that did not take into account the value of the corporate governance reforms. They referred to situations where the settlement did not, as it does in this case, provide both for a monetary payment to the corporation by its directors and a non-monetary corporate benefit. *See* Pet. Br. 9 n.10.

When petitioners appeared at the settlement hearing in July 1977, they alluded to the potential for collusion in derivative and class action settlements. They admitted, however, that they had no evidence of collusion, App. 338, and the district court judge made an express finding that there was "no basis for claims of collusion. Just none. These people have dealt with each other professionally and at arm's length." App. 347. The district court did have evidence—the written record—of the history of the litigation, the reasons for the settlement and the value of the settlement. Based on this record, briefs and oral arguments, the district court approved the settlement as fair, reasonable and adequate. Pet. App. 12a.[7] Citing expert affidavits as to the value of the corporate governance reforms, the district court awarded plaintiffs attorneys' fees and expenses totaling $3,920,000. Pet. App. 17a. One week later, petitioners filed their notice of appeal from the district court's final judgment and orders.

SUMMARY OF ARGUMENT

1. In *Marino v. Ortiz*, 484 U.S. 301, 304 (1988), this Court said:

> The rule that only parties to a lawsuit, or those that properly become parties, may appeal an adverse judgment, is well settled. The Court of Appeals suggested that there may be exceptions to this general rule, primarily "when the nonparty has an interest that is affected by the

[7] In addition to the written evidentiary record and oral arguments, plaintiffs' financial expert, R. Alan Miller, was present for the hearing.

> trial court's judgment." We think the better practice is for such a nonparty to seek intervention for purposes of appeal; denials of such motions are, of course, appealable.

Relying upon this language, Fed.R.App.P. 3(c), and its own earlier decision in *Brand Name Prescription Drugs*,[8] the court below held that Fed.R.Civ.P. Rule 23.1 objectors who had not sought to intervene could not appeal from a district court's final judgment approving a derivative suit settlement. In this Court, petitioners and their *amici* advance a wide range of arguments seeking reversal. Some are plainly irrelevant. The repeated emphasis (Pet. Br. 13-16, 33-34) on the alleged importance of the objectors' "monitoring" function surely cannot magically transform "objectors" into "parties". Other arguments appear in a contradictory fashion. The various briefs inform the Court both that an intervention requirement is a meaningless formality, and that such a requirement is so burdensome as to deter the appearance of objectors.

2. Like this Court's Rules 12 and 14, Rule 3(c) reflects the principle that only parties may appeal. *See also* 28 U.S.C. §1254(1), which directly governs this proceeding and which restricts petitioners to "any party". Accordingly, petitioners must demonstrate party status. Although petitioners and their principal *amicus*, the United States, vary in expositional style, both in

[8] *In re Brand Name Prescription Drugs Antitrust Litigation*, 115 F.3d 456 (7th Cir. 1997). There, the court, relying upon *Marino*, held that objectors in a class action who had not intervened could not appeal. The court below believed that *Brand Name*'s reasoning applied *a fortiori* in a derivative context. (Pet. App. 4a-6a)

the end draw upon two sources: Rule 23.1 and the decisions allowing persons not named in the pleading captions to appeal—"quasi parties" in the government's terminology[9] or, more appropriately, "ancillary parties". Petitioners insist that they are *de facto* parties by virtue of responding to a Rule 23.1 notice (Br. 19), and also that they fall within the case law permitting non-named parties to appeal. Br. 25-27. Similarly, the government argues that Rule 23.1 "quasi-party precedents do furnish support for appealability" (Br. 16), which is reflected by the language of Rule 23.1 itself. Br. 12-15.

But reliance upon either Rule 23.1 or the "quasi party" doctrine is misplaced.

(a) *Rule 23.1.* (pp. 15-17, *infra*). The government acknowledges that at common law some courts held that nonparty shareholders had no right to notice of a derivative action settlement. Br. 19-20. Rule 23.1 alters that legal landscape, providing stockholders with a right to notice of the proposed settlement and court approval, which in practice carry with them a right to appear for the purpose of objecting. In a Rule 23.1 proceeding, however, an objector does not participate as a party. The shareholder cannot dictate litigation strategy, settle the litigation, or represent the corporation on any issue in the litigation. He can only object. Nothing in Rule 23.1's language or history remotely suggests that the Rule was also intended *implicitly* to confer appeal rights in addition to the two rights that it confers upon shareholders.

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[9] The term quasi party appears in Justice Story's opinion in *West v. Randall*, 29 F.Cas. 718, 722-23 (C.C. D.R.I. 1820).

(b) *Ancillary or Non Caption Parties.* (pp. 17-20, *infra*). Neither Rule 3(c) nor this Court's Rule 12 defines "party" but, as the case law and this Court's Rule 14(b) make clear, this term properly includes persons other than those listed in the pleading captions. The decisions of this Court demonstrate that "ancillary" parties can be grouped into three general categories. *First*, where the appellant is himself the direct object of a judicially enforceable order, such as an injunction or a contempt citation. Second, where the court purports directly to affect legally established rights or duties of named persons, such as determining ownership rights. As *Marino v. Ortiz* makes clear, however, the judicial order must do more than simply disadvantage the would-be appellant. *See also Martin v. Wilks*, 490 U.S. 755 (1989). Rather, the order must operate directly upon the rights or duties of named or identifiable persons. Third, where (as *Marino v. Ortiz* makes plain) the appellant has unsuccessfully sought to intervene in the proceeding.

Neither of the first two categories is applicable here. Rule 23.1 provides for the issuance of a notice, not a summons. (Compare Fed.R.Civ.P. Rule 4). Objectors are not "summoned" to the court, any more than are absent class members who receive a comparable notice under Rule 23(e). *Phillips Petroleum Co. v. Shutts*, 472 U.S. 797, 808-811 (1985). Shareholders can ignore the notice, *and if they do, their own legal rights are not affected.* The government's unsupported argument that the objecting stockholder under Rule 23.1 asserts a "personal right" (Br. 16) is wrong. A Rule 23.1 proceeding itself concerns only the rights of the corporation and all of its stockholders, not the rights of or losses suffered by indi-

vidual stockholders. *Kamen v. Kemper Fin. Servs., Inc.*, 500 U.S. 90, 95 (1991).

(c) *State Law.* An *amicus* contends that state law governs the party status of objectors. (pp. 21-22, *infra*). This issue is not "fairly included" within the question presented (Rule 14.1(a) of the Rules of this Court), and, in any event, is implausible.

3.(a) The distinction between the status of objectors and intervenors has much to commend it. (pp. 22-25, *infra*). A requirement that an objector move to intervene neither reflects a meaningless formality nor creates an unwarranted obstacle. In a derivative suit, the shareholder plaintiff fights for the right to speak for the corporation and then to proceed with the corporation's claims. *Ross v. Bernhard*, 396 U.S. 531, 538 (1970). An intervenor assumes at least some responsibilities and makes some commitments. An objector, by contrast, makes no commitments and assumes no responsibilities. Objectors are not all cut from the same bolt of cloth. Some undertake serious work; others appear in a more or less desultory fashion. Intervention proceedings thus serve as a screening device to deter frivolous or "hold up" appellate challenges to a settlement. If the distinction between objectors and parties is to be altered, it is for Congress to determinate, or for the rule-making process.

(b) Petitioners' argument that appealability without intervention is necessary to prevent collusion is meritless. (pp. 25-27, *infra*). It assumes not only that a district court will rubber-stamp a "collusive settlement" in the face of cogent, well-founded objections and deny a well-founded motion to intervene, but also that the

court of appeals will not carefully review the district court's decisions. If this is truly the situation, it will make no difference whether a nonparty could appeal without seeking to intervene. Either way, the ultimate appeal would be futile. Petitioners' additional argument that an intervention requirement would subject them to burdens, *e.g.*, discovery, is, at best, speculative, as the Court noted of similar claims in *Phillips Petroleum Co. v. Shutts*, 472 U.S. at 810 n.2, and in any event is irrelevant.

ARGUMENT

This case has had extensive briefing with respect to the meaning and content of Rule 23.1, and this Court's ancillary party cases. We see no reason to duplicate that elaborate and meticulous discussion. Rather our submission emphasizes the points that we think are most salient. They reduce to two: only parties can appeal and objectors are not parties.

I. Only Parties Can Appeal and Objectors Are Not Parties.

"The rule that only parties to a law suit, or those that become parties, may appeal an adverse judgment, is well settled." *Marino v. Ortiz*, 484 U.S. at 304. Petitioners' statement that federal courts "routinely permit nonparty appeals" in a wide variety of circumstances (Br. 25-26) is wrong. It rests upon the implicit assumption that only the persons actually named in the caption of the pleadings are properly considered "parties". This is, as we shall show, an error. The authorities actually cited by petitioners and the government involve

situations in which the courts properly viewed persons not named in the captions as ancillary parties. But they provide no assistance to petitioners. Petitioners are objectors. Objectors are not parties. Objectors are just that: objectors.

Rule 3(c) clearly embodies the background premise that only a "party or parties" can appeal. *Marino v. Ortiz*, 484 U.S. 301, 304; *see also* 28 U.S.C. §1254(1). Like this Court's Rule 12, Rule 3(c) itself does not define that term. The case law recognizes that the term "party or parties" properly embraces more than the persons named in the pleading caption. As does this Court's Rule 14.1(b).[10] But as Rule 12 makes clear (to say nothing of 28 U.S.C. §1254(1)), this Court is concerned with the rights of parties. Only parties may petition for certiorari, Rule 12.4, and "all parties to the proceeding in the Court below are deemed parties . . ." Rule 12.6.

To establish their right to appeal to the court of appeals or to this Court, petitioners must establish that they are parties. They cannot do so. Rule 23.1 does not help them and neither do the cases treating persons not named in the pleading caption as parties.

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[10] Rule 14.1 provides:

> A petition for a writ of certiorari shall contain, in the order indicated:
>
> (b) A list of all parties to the proceeding in the court whose judgment is sought to be reviewed (unless the caption of the case contains the names of all the parties), and a list of parent companies and nonwholly owned subsidiaries as required by Rule 29.6.

A. Rule 23.1.

Rule 23.1 can only be understood against the background of a derivative suit. A derivative suit is, in essence, two suits. *Daily Income Fund, Inc. v. Fox*, 464 U.S. 523, 529 n.4 (1984). The first is an effort by a shareholder to establish the authority to speak for the corporation, when the corporation has failed to enforce a right it has. The second, once the authority is established, consists of the shareholder's efforts, in the language of Rule 23.1, "to enforce the right of a corporation." *See Kamen v. Kemper Fin. Servs., Inc.*, 500 U.S. 90, 95-96 (1991). In a derivative action, a shareholder has an economic interest, the value of his shares, but the shareholder brings the proceeding solely in the interests of the corporation and its shareholder owners. In discharging that obligation, a derivative plaintiff may seek to settle or dismiss the case. In such circumstances, Rule 23.1 gives shareholders two rights: the right to notice and the right to court approval. These are valuable rights designed to prevent abuse. But these rights do not confer party status upon the objector. If the district court rejected a settlement, an objector could not force the corporation to adopt a different settlement and could not prosecute or dismiss the case. Objectors bear none of the rights and responsibilities of a party. Indeed, they have no rights whatsoever if the district court dismisses the case involuntarily. *Burks v. Lasker*, 441 U.S. 471, 485-86 n.16 (1978). If objectors seek greater rights, they must move to intervene under Rule 24. Unless they do so, objectors remain objectors, not parties.

Petitioners seek to avoid this obvious difficultly by insisting they were "summoned" to appear in district

court.[11] They thereby seek to assimilate their status to that of a civil defendant. Under Fed.R.Civ.P. 4, a summons issues only to defendants and certain plaintiffs joined as such under Fed.R.Civ.P. 19. *See Chase Nat'l Bank v. City of Norwalk*, 291 U.S. 431, 441 (1934), cited with approval in *Martin v. Wilks*, 490 U.S. at 763. Rule 23.1 *authorizes the issuance of a notice, not a summons.*[12] That notice imposes *no* legal obligation upon the shareholder. The shareholder can ignore it, and if he does, none of his own legal rights is determined. Petitioners' effort to assimilate their status to that of a defendant is no more convincing than it was when made in *Phillips Petroleum Co. v. Shutts*, 472 U.S. 797, 808-811 (1995). There, this Court rejected an attempt by nonresident class members to analogize their status for purposes of *in personam* jurisdiction to that of a nonresident defendant. The Court stressed the many differences between the two and stated that, in reality, the class member "is not required to do anything". *Id.* at 810. *See also* Henry P. Monaghan, *Antisuit Injunctions and Preclusion Against Absent Nonresident Class Members*, 98 COLUM.L.REV. 1148, 1162-1173 (1998) (discussing this aspect of *Shutts*). The same is true here.

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[11] In the Question Presented in their brief on the merits, petitioners restate the question as follows: "Whether a shareholder who, pursuant to Federal Rule of Civil Procedure 23.1, is summoned to appear in federal district court and present objections to a proposed dismissal or settlement of a derivative action must also intervene pursuant tc Federal Rule of Civil Procedure 24 in order to appeal an adverse decision."

[12] The government, relying on *Cohen v. Young*, 127 F.2d 721, 724 (6th Cir. 1942), seems to endorse the "summons" argument. Br. 6.

Petitioners, however, undercut their "summons" argument, for the key fact upon which they rely is not simply the existence of the Rule 23.1 notice to shareholders, but the fact that they responded to the court's "invitation". Br. 19. But their acceptance of the court's "invitation" cannot transform a Rule 23.1 "objector" into a "party." *See*, for example, *Grant v. United States*, 227 U.S. 74, 79 (1913). An objector appears in court solely in the interest of the corporation, but as an objector. The language of Rule 23.1 does not confer party status on him. Of course, petitioners do not want any burdens that party status brings. They are really asking for the status of "super parties", that is to say, to have all the rights of a party in gaining access to the appellate court, but without shouldering any of the responsibilities. Rule 23.1 does not afford them this luxury.

B. Ancillary or Non Caption Parties.

As we have noted, neither Rule 3(c) nor this Court's Rule 12 defines "party", but as the case law and this Court's Rule 14(b) make clear, this term properly includes persons other than those listed in the pleading captions.[13] The government insists that use of the category of ancillary party "should be sparing indeed". Br. 16. This Court's[14] decisions support grouping "ancil-

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[13] Petitioners argue that 28 U.S.C. §1291 does not mention a party requirement. But 28 U.S.C. §1254(1) does. Moreover, it seems highly unlikely that §1254(1) provides this Court with less jurisdiction than §1291 gives to the court of appeals.

[14] Interestingly, in massing their ancillary party cases, petitioners rely almost exclusively on lower court decisions and the views of a treatise. *See* Br. 25-26. By contrast, the govern-

(continued...)

lary" parties into three general categories. First, where the appellant is himself the direct object of a judicially enforceable order, such as an injunction or a contempt citation. *United States v. Nixon*, 418 U.S. 683 (1974). Second, where the court purports directly to affect legally established rights or duties of named persons. *E.g.*, *Kneeland v. American Loan & Trust Co.*, 136 U.S. 89, 94 (1890); *Blossom v. The Milwaukee Railroad*, 68 U.S. 655, 655-56 (1863). In these circumstances, the judicial order must do more than simply disadvantage the would-be appellant, as *Marino v. Ortiz*, 484 U.S. 301, makes plain. Rather, it must operate directly upon the rights or duties of named persons. Third, where the appellant has unsuccessfully sought to intervene in the proceeding. *Id.*

Neither of the first two categories is applicable here. As discussed above, objectors are not "summoned" to the court, any more than are absent class members in a Rule 23 proceeding who receive a comparable notice under Rule 23(e). Shareholders can ignore the notice, *and if they do, their own legal rights are not affected.* The government's unsupported argument that the objecting stockholder under Rule 23.1 asserts a "personal right" (Br. 16) is quite misleading. As we have noted, as a stockholder, the objector may have an economic interest sufficient to satisfy art. III, but a Rule 23.1 proceeding concerns only the rights of the corporation,

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[14] (...continued)
ment confines its discussion to the decisions of this Court. Br. 16-18. In this brief, like the government, we focus on the decisions of this Court.

not losses suffered by individual stockholders. *Kamen v. Kemper Fin. Servs., Inc.*, 500 U.S. at 95.

Petitioners' reliance (Br. 21) upon this Court's decision in *Johnson v. Manhattan Railway Co.*, 289 U.S. 479, 495 (1933) is misplaced. *Johnson* arose in unusual circumstances: a bitter jurisdictional clash between a senior circuit judge, sitting in the district court, and the district judges over appointment of equity receivers. So far as relevant here, this Court rejected a collateral attack upon a proceeding in which the senior circuit judge had entered an order continuing the appointment of a temporary receiver. In a paragraph explaining why the second proceeding was a collateral and not a direct attack on the order entered by the circuit judge, this Court said the new litigants could have appeared before the circuit judge to oppose the continuance of the receivership. The Court then added that, "had the receivership been continued without giving effect to [their] objections they would have been entitled to appeal." This statement is viewed in isolation, is *dictum*, and it was certainly not a matter upon which the Court focused. None of the four circuit opinions the Court cited supports the statement, even in the receivership context.[15] Moreover, on the very next page of the

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[15] In *Christian v. R. Hoe*, 63 F.2d 218 (2d Cir. 1933), for example, the appellant owned shares and a note. He did not appear as a shareholder. Rather, he "appeared in his own behalf and in behalf of other note holders". In *Mitchell v. Lay*, 48 F.2d 79, 84-85 (9th Cir. 1931), a judgment had been entered against the appellant. "The judgment therein rendered was as to him final and appealable as such." *Id.* at 85. In *Kingsport Press, Inc. v. Brief English Systems, Inc.*, 54 F.2d 497 (2d Cir. 1931), a creditor was allowed to appeal an order
(continued...)

Court's opinion, the Court discusses the intervention rights the litigants would have had in the proceeding before the circuit judge. *Id.* at 496. Thus *Johnson* does not hold that an objector could appeal without seeking intervention. It is best read as recognizing a right of appeal when the litigants actually intervened in the proceeding before the senior circuit judge.

Whatever role the *Johnson* statement may have in the reorganization and receivership context, however, it cannot be extended to a Rule 23.1 proceeding. To do so would be inconsistent with the language and policy of the Rule. Moreover, such an extension would be inconsistent with the statutes and rules governing the subject matter jurisdiction of the courts of appeals and of this Court. This Court has emphasized just recently the imperative nature of the obligation that lower federal courts observe statutory and constitutional restrictions on subject matter jurisdiction. *Steel Co. v. Citizens for a Better Environment*, 118 S.Ct. 1003, 1012-16 (1998). *See also Lexecon, Inc. v. Milberg Weiss Bershad Hynes & Lerach*, 118 S.Ct. 956 (1998).

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[15] (...continued)
appointing a receiver. There was much discussion of the law governing the appointment of a receiver on the application of a simple contract creditor, but no issues of appellate jurisdiction were discussed. Finally, in *Blake v. District Court*, 59 F.2d 78 (9th Cir. 1932), a percentage holder of oil and gas leases sought appellate relief under the All Writs Act. 28 U.S.C. §1651(a). Relief was denied because the petition was an improper end run around the statute governing appeals to the court of appeals (28 U.S.C. §1291), and petitioner should have participated in the district court proceeding.

C. State Law.

The *amicus* brief submitted by Professors Hamermesh and McManamon contends that, in derivative actions, state law provides the controlling rule of decision as to whether an objector may appeal without intervention. The claim seems to be that Rule 23.1 "incorporates" this "substantive" provision of Delaware law. Br. 13. If it does not, the professors insist, Rule 3(c) would be invalid under the Enabling Act, 28 U.S.C. §2072, because it "abridge[d] . . . [a] substantive right". Br. 12. This issue was not raised by the petition for *certiorari* and it cannot be said to be "fairly included" within the grant.[16] What is more an *amicus* ordinarily has no standing to enlarge the question presented by petitioner. *United States v. Dion*, 476 U.S. 734, 746 (1986). Most importantly, the issue was not even considered by the court below. *Matsushita Elec. Indus. Co. v. Epstein*, 516 U.S. 367, 379 n.5 (1996). If the issue raised by the *amicus* brief were thought to be pertinent, the writ should be dismissed as improvidently granted because the issue is not presented by this record. *See* Robert L. Stern, *et al.*, SUPREME COURT PRACTICE 259 (7th ed. 1993) (collecting cases).

Suffice it for our purposes to say that on its face the professors' analysis seems implausible.[17]

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[16] Rule 14.1(a) of this Court's rules states that, "Only the questions set out in the petition, or fairly included therein, will be considered by the Court."

[17] To the extent that Rule 3(c)—or its background premise that only parties can appeal—excludes certain persons from an appeal, it is surely well within the constitutional authority of
(continued...)

II. Intervention Is an Important Requirement.

A. Intervention Serves a Meaningful Function.

Requiring that a shareholder who wants to appeal first seek to intervene has the beneficial effect of deterring frivolous or obviously self-interested appeals. Objectors come in all sizes and shapes. Some make a substantial commitment of time and energy; others do not. Should one shareholder be able to delay implementation of a settlement for a year or more by simply filing a technical objection, by sending a bare-boned opposition letter to the court, or by arguing that the settlement is not what he would have done? Suppose that three shareholders desire different and conflicting

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[17] (...continued)
Congress to so provide. That was settled long ago. In *Sheldon v. Sill*, 49 U.S. 441 (1850), this Court sustained an exclusion of assignees from a district court's diversity jurisdiction. The Court there recognized that the jurisdiction of the inferior federal courts is prescribed by Congress. *Id.* at 448-49. And, of course, the histories of diversity and federal question jurisdiction are replete with the exclusion of certain categories of would-be litigants without regard to the content of state law. The claim that failure to follow Delaware "substantive" law would render Rule 3(c) inconsistent with the Enabling Act is also incorrect. A federal rule that said that a non intervening objector is not a party is clearly procedural in nature, within the teachings of this Court's cases. *Hanna v. Plummer*, 380 U.S. 460, 469-74 (1965); *Walker v. Armco Steel Corp.*, 446 U.S. 740, 750-53 (1980). Congress could, of course, absorb state law on this point. *See*, for example, Fed.R.Civ.P. 17(b). But the *amicus* briefs provide no evidence that it has done so here. Quite to the contrary. So far as "party status" is concerned, Rule 23.1's "contemporaneous ownership" requirement imposes restrictions on derivative suit plaintiffs as a matter of federal policy wholly irrespective of the content of state corporate law. *Daily Income Fund, Inc. v. Fox*, 464 U.S. at 531 n.6.

results. Under Rule 23.1, these shareholders may be entitled to file an objection and even appear to have their day in court. But that is all that it is. Without a more substantial commitment, they should not be accorded a further opportunity to hold up implementation of a settlement to which the parties have agreed and which a district court has approved. Petitioners' assertion that their procedure would not increase the number of appeals (Br. 37-38) is wide of the mark. Quantity is not the issue. A requirement of intervention will at least help to deter meritless or self-interested appeals with all of their attendant costs and delays.[18]

There is another policy advanced by an intervention requirement: certainty as to when the litigation is over. If no objector moves to intervene and the district court approves the settlement and enters judgment, the parties can be certain that the litigation is at an end.

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[18] Of course, as has been recognized, objectors are not immune from self-interest or ignorance. Patrick Woolley, *Rethinking the Adequacy of Adequate Representation*, 75 TEX.L.REV. 571, 618 (1997) ("By filing or threatening to file an objection to the settlement a class member may be able to 'extort' a settlement"); Jonathan R. Macey and Geoffrey P. Miller, *The Plaintiff's Attorney's Role in Class Action and Derivative Litigation: Economic Analysis and Recommendations for Reform*, 58 U.CHI.L.REV. 1, 46 (1991) (Objectors are often either disgruntled plaintiffs' lawyers or uninformed class members). For a discussion of the self-interest and obstruction that objectors may bring to the proceedings, *see Holden v. Burlington Northern, Inc.*, 665 F. Supp. 1398, 1428-31 (D. Minn. 1987). In this case, the institutional investor *amici* argue that, although they may lack the time and resources to monitor litigation (Br. 10-15), they should have the right to appeal if the district court judge does not agree with their views, no matter how uninformed and incorrect.

Intervention simply reflects the dual nature of a derivative action. A derivative action permits a shareholder to "step into the corporation's shoes and to seek in its right the restitution he could not demand in his own." *Cohen v. Beneficial Indus. Loan Corp.*, 337 U.S. 541, 548 (1949). Intervention properly focuses the court and the parties on the threshold issue in a derivative action, that is, whether the plaintiff, including the intervening plaintiff, has the right to sue on behalf of the corporation. *Ross v. Bernhard*, 396 U.S. 531, 538 (1970). When properly viewed in the context of what a derivative suit is about, intervention is quite obviously not a meaningless formality or an unwarranted obstacle. Because only a shareholder who speaks for the interests of the corporation is entitled to litigate and, therefore, to appeal, it is logical to require that the shareholder first make a showing either that the named plaintiff does not adequately represent the interests of the corporation and all its shareholders, and that the objector does, Rule 24(a); or, at least, that the objecting shareholder seeks to represent the interests of the corporation in objecting to the settlement and has a claim in common with the main action, Rule 24(b). This threshold issue is also one that the court of appeals should be able to focus on first, regardless of which way the district court rules in what has become a dispute over which shareholder best represents the interests of all and should be heard on behalf of the corporation.

This case is not the appropriate vehicle for deciding the policy argument of petitioners and their *amici* that objectors can play an important role in settlement proceedings so long as they are allowed to proceed without more. If Rule 23.1 or Fed.R.App.P. 3(c) is to be

rewritten, *see Martin v. Wilks*, 490 U.S. 755, 767 (1989), then the rulemaking process that 28 U.S.C. §2072 provides for should be invoked. *Amchem Prods., Inc. v. Windsor*, 117 S.Ct. 2231, 2248 (1997). If jurisdictional statutes, for example 28 U.S.C. §1254(1), are to be amended, Congress must undertake that task. Rulemaking, whether under the auspices of Congress or the Court, will allow the full consideration of the potentials for abuse that exist if *any* shareholder who objects—even by sending a letter—to any part of any settlement can appeal and delay for a year or more implementation of a settlement that other shareholders have accepted.

B. An Intervention Requirement Does Not Promote Collusive Settlements or Impose Undue Burdens.

Petitioners argue that appeals by nonparty objectors are necessary to prevent collusive or unfair settlements. They express great concern that district court judges charged with the responsibility for deciding whether a settlement is fair or adequate will be misinformed or uninformed. Assuming for argument's sake that petitioners are correct about the state of affairs without objectors, this argument further assumes that federal district court judges will abandon their responsibilities as guardians of the class and will rubber stamp a "collusive settlement" in the face of cogent, well-founded objections. Petitioners totally discount the possibility

that district courts consider and respond appropriately to valid objections.[19]

Of course, all of petitioners' expressed concerns could readily be addressed by a motion to intervene. If denied, objectors could appeal this denial just as they could appeal the approval of the settlement. Petitioners, however, argue, inconsistently, that district courts will deny motions to intervene—a result that could, of course, be appealed—or that the courts may instead grant these motions, subjecting them to the burdens, risks and responsibilities that parties have, but that petitioners are unwilling to assume. The fear of discovery is speculation, as this Court has already observed of similar fears, *see Phillips Petroleum Co. v. Shutts*, 472 U.S. at 810 n.2, and would appear totally illusory in the case of an intervention for purposes of appeal. Similarly, any additional pleading burdens are certainly not unduly harsh for someone who seeks the time and attention of a court of appeals. It is also an obligation commensurate with the ability of the objecting shareholder to delay the implementation of a settlement. Finally, the argument that not all objectors can intervene, if correct, would not justify a different approach. If an objector cannot be a party under Rule 23.1 and, therefore, could not intervene, it is appropriate to foreclose an appeal, because this shareholder by definition cannot represent the interests of the corporation.

[19] Petitioners provide no statistics on the total number of settlements that district courts have rejected. The sampling of appeals they do present (Br. 37-38) suggests that more settlements are rejected at the district court level than are approved and reversed on appeal. The suggestion of certain institutional investor *amici* (Br. 17) that lower court disapprovals are related to the threat of an appeal is pure speculation.

CONCLUSION

For the reasons stated, this Court should affirm the judgment of the Court of Appeals for the Seventh Circuit.

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No. 97-1732

IN THE
Supreme Court of the United States
OCTOBER TERM, 1998

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM, *et al.*,
Petitioners,

v.

PAUL FELZEN, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

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BRIEF FOR RESPONDENT ARCHER DANIELS MIDLAND COMPANY

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QUESTION PRESENTED

Whether a nonparty shareholder who appears, in response to notice provided under Federal Rule of Civil Procedure 23.1, to present objections to a proposed dismissal or settlement of a derivative action may appeal an adverse decision even though the shareholder has not been formally made a party to the action.*

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* This is the question presented in the petition, Pet. Cert. i, on which this Court granted certiorari, J.A. 351. It is not the question as stated in the Brief for Petitioners, at i.

LIST OF PARTIES IN THE COURT OF APPEALS

California Public Employees' Retirement System and Florida State Board of Administration were not parties in the District Court. They filed a notice of appeal describing themselves as "Objectors . . . each of whom is entitled to appeal." J.A. 349. They did not move to intervene in the Court of Appeals, and were not granted intervention by that Court, which dismissed their appeal.

Parties to the judgment of the District Court from which the objectors sought to appeal were Paul Felzen; Sandra Esner; Archer Daniels Midland Company; the following directors of Archer Daniels Midland Company: Dwayne O. Andreas, Gaylord O. Coan, F. Ross Johnson, M. Brian Mulroney, Robert S. Strauss, John K. Vanier, and O. Glenn Webb; and the following former directors of Archer Daniels Midland Company: Lowell W. Andreas, Martin Andreas, Michael D. Andreas, Shreve M. Archer, Jr., Ralph Bruce, Howard G. Buffett, John H. Daniels, Ray A. Goldberg, H. D. Hale, James R. Randall, and Margaretta Rockefeller.

LIST PURSUANT TO RULE 29.6

Respondent Archer Daniels Midland Company is a publicly held corporation. It has no parent companies. Its non-wholly-owned subsidiaries are Alfred C. Toepfer International, Compagnie Industrielle et Financière, Consolidated Nutrition, L.C., Gruma, S.A. de C.V., and Oelmuhle Hamburg AG.

TABLE OF CONTENTS

	Page
QUESTION PRESENTED	i
LIST OF PARTIES IN THE COURT OF APPEALS	ii
LIST PURSUANT TO RULE 29.6	ii
TABLE OF AUTHORITIES	vi
JURISDICTION	1
STATUTES AND RULES INVOLVED	1
STATEMENT	1
A. Proceedings in the District Court	1
1. The Complaints	1
2. The Proposed Settlement	2
3. Objections	3
4. The Fairness Hearing	5
5. The Notice of Appeal	6
B. Proceedings in the Court of Appeals	6
SUMMARY OF ARGUMENT	8
ARGUMENT	11
I. THE FEDERAL RULES DO NOT AUTHORIZE APPEALS BY NON-PARTIES IN SHAREHOLDER DERIVATIVE ACTIONS	11
A. Civil Rule 23.1 Specifies the Procedural Rights of Non-Party Shareholders	11
B. Civil Rule 24 Prescribes the Procedure and Standards for Intervention	15
C. Appellate Rule 3 Specifies That Appeals Are by Parties	19

TABLE OF CONTENTS—Continued

	Page
II. REJECTION OF NON-PARTY APPEALS LONG PRECEDED THE FEDERAL RULES..	21
A. *Marino* v. *Ortiz* Confirms More Than a Century of This Court's Decisions	21
B. Most Courts of Appeals Have Applied the Rule Reiterated in *Marino*	26
C. CalPERS and FSBA Did Not Become Parties Without Intervention	30
1. They Were Not Made Parties *De Facto*..	30
2. They Were Not Summoned or Ordered....	31
3. They Were Not Parties in an Ancillary Proceeding	33
D. Developments in English Chancery Did Not Alter the Established Rule	36
III. NON-PARTY APPEALS WOULD NOT BE CONFINED TO DERIVATIVE ACTIONS....	39
A. Non-Party Shareholder Appeals Would Mean Non-Party Appeals in Class Actions	39
B. Non-Party Appeals Would Unsettle Litigation of Many Other Kinds	40
IV. CALPERS' AND FSBA'S POLICY ARGUMENTS ARE INCOMPLETE AND MISDIRECTED	41
A. CalPERS' and FSBA's Policy Arguments Rest on Flawed Assumptions and Ignore Competing Policies	41
1. CalPERS' and FSBA's Arguments Assume Inadequate Representation and Faulty Judicial Performance	42
2. Non-Party Appeals Are Not Essential To Protect Objecting Shareholders.....	44

TABLE OF CONTENTS—Continued

	Page
3. Non-Party Appeals Would Make Settlements More Difficult, Costly and Uncertain	45
4. Non-Party Appeals Would Proliferate and Confuse Appellate Litigation	47
B. Policy Arguments Should Be Directed to Congress or the Rules Advisory Committees	47
CONCLUSION	50
ADDENDUM	
Title 28 United States Code (§§ 1254, former 1254)	1a
Federal Rules of Civil Procedure (Rules 23, 23.1, 24, former Rule 73)	3a
Federal Rules of Appellate Procedure (Rules 3, 4)	10a
Federal Equity Rules (Rule 94 of 1882, Rules 27, 37, 38, 39 of 1912)	17a

TABLE OF AUTHORITIES

Cases: Page

Ace Heating & Plumbing Co. v. *Crane Co.*, 453 F.2d 30 (3d Cir. 1971) 27
Ackerman v. *Kassar*, 5 F.3d 534 (9th Cir. 1993) 43
Adams v. *Morton*, 581 F.2d 1314 (9th Cir. 1978), *cert. denied sub nom. Gros Ventre Tribe* v. *United States*, 440 U.S. 958 (1979) 31
Amchem Prods., Inc. v. *Windsor*, 117 S. Ct. 2231 (1997) 15, 49
Arizonans for Official English v. *Arizona*, 520 U.S. 43 (1997) 17
In re Archer Daniels Midland Co. Derivative Litig., No. 14403 (Chan. Ct., New Castle Co., Del.) 2
In re Asbestos Litigation, 90 F.3d 963 (5th Cir. 1996), *vacated*, 117 S. Ct. 2503 (1997), *on remand*, 134 F.3d 668 (5th Cir.), *cert. granted sub nom. Ortiz* v. *Fibreboard Corp.*, 118 S. Ct. 2339 (1998) (No. 97-1704) 42
Baker v. *Biddle*, 2 Fed. Cas. 439 (C.C.E.D. Pa. 1831) (No. 764) 36
Baker v. *Wade*, 769 F.2d 289 (5th Cir. 1985) (*en banc*), *cert. denied*, 478 U.S. 1022 (1986) 21
Bank of Nova Scotia v. *United States*, 487 U.S. 250 (1988) 15
Bayard v. *Lombard*, 9 How. 530 (1850) 22
Bell Atlantic Corp. v. *Bolger*, 2 F.3d 1304 (3d Cir. 1993) 8, 27, 29, 30, 43
Bigelow v. *Old Dominion Copper Mining & Smelting Co.*, 225 U.S. 111 (1912) 24
Blatt v. *Dean Witter Reynolds Intercapital, Inc.*, 732 F.2d 304 (2d Cir. 1984) 43
Blossom v. *Milwaukee R.R.*, 1 Wall. 655 (1864) 34, 35
Boyle v. *Zacharie*, 6 Pet. 648 (1832) 33
In re Brand Name Prescription Drugs Antitrust Litig., 115 F.3d 456 (7th Cir. 1997) 7, 28, 48
Brotherhood of R.R. Trainmen v. *Baltimore & O.R.R.*, 331 U.S. 519 (1947) 20
Burlington N.R.R. v. *Woods*, 480 U.S. 1 (1987) 21
Business Guides, Inc. v. *Chromatic Communications Enterprises, Inc.*, 498 U.S. 533 (1991) 15

TABLE OF AUTHORITIES—Continued

Page

Byrd v. *Blue Ridge Rural Elec. Coop., Inc.*, 356 U.S. 525 (1958) 21
Carson v. *American Brands, Inc.*, 450 U.S. 79 (1981) 45
Cathcart v. *Robinson*, 5 Pet. 264 (1831) 36
Chambers v. *NASCO, Inc.*, 501 U.S. 32 (1991) 15
City Partnership Co. v. *Atlantic Acquisition Ltd. Partnership*, 100 F.3d 1041 (1st Cir. 1996) 43, 47
Clark v. *Lomas & Nettleton Financial Corp.*, 625 F.2d 49 (5th Cir. 1980), *cert. denied*, 450 U.S. 1029 (1981) 43
Cockburn v. *Thompson*, 16 Ves. Jun. 321, 33 Eng. Rep. 1005 (Ch. 1809) 36, 37
Ex parte Cockcroft, 104 U.S. 578 (1882) 22
Cohen v. *Beneficial Indus. Loan Corp.*, 337 U.S. 541 (1949) 48
Cohen v. *Young*, 127 F.2d 721 (6th Cir. 1942) 26, 27, 28, 29, 30, 32
Commanding Officer v. *United States ex rel. Bumanis*, 207 F.2d 499 (6th Cir. 1953) 20
Connor v. *Peugh's Lessee*, 18 How. 394 (1856) 22
Croyden Assocs. v. *Alleco, Inc.*, 969 F.2d 675 (8th Cir. 1992), *cert. denied sub nom. Harry & Jeannette Weinberg Foundation, Inc.* v. *Croyden Assocs.*, 507 U.S. 908 (1993) 24, 29, 44
Ex parte Cutting, 94 U.S. 14 (1877) 22
Daily Income Fund, Inc. v. *Fox*, 464 U.S. 523 (1984) 11
Donovan v. *Robbins*, 752 F.2d 1170 (7th Cir. 1985) 45
Duke of Bedford v. *Ellis*, L.R. [1901] A.C. 1 (H.L.) 37
EEOC v. *Pan American World Airways, Inc.*, 897 F.2d 1499 (9th Cir.), *cert. denied sub nom. Keith* v. *EEOC*, 498 U.S. 815 (1990) 29
Eisen v. *Carlisle & Jacquelin*, 417 U.S. 156 (1974) 15, 25, 45
Esner v. *Andreas, et al.*, No. 95 CH 6623 (Cir. Ct., Cook Co., Ill.) 2

TABLE OF AUTHORITIES—Continued

	Page
Evans v. *Jeff D.*, 475 U.S. 717 (1986)	44
Felzen v. *Andreas, et al.*, No. 95 C 4006 (N.D. Ill.)	2
Firestone Tire & Rubber Co. v. *Risjord*, 449 U.S. 368 (1981)	8
First Iowa Hydro Elec. Coop. v. *Iowa-Illinois Gas & Elec. Co.*, 245 F.2d 630 (8th Cir. 1957)	20
Galloway v. *United States*, 319 U.S. 372 (1943)	36
Gasperini v. *Center for Humanities, Inc.*, 518 U.S. 415 (1996)	21
In re General Tire & Rubber Co. Securities Litig., 726 F.2d 1075 (6th Cir. 1984), *cert. denied sub nom. Schreiber* v. *Gencorp, Inc.*, 469 U.S. 858 (1984)	43
Giffard v. *Hort*, 1 Sch. & Lef. 386 (Ir. Ch. 1804, H.L. 1805)	38
Girsh v. *Jepson*, 521 F.2d 153 (3d Cir. 1975)	44
Goldsholl v. *Shapiro*, 417 F. Supp. 1291 (S.D.N.Y. 1976)	43
Gottlieb v. *Wiles*, 11 F.3d 1004 (10th Cir. 1993)	28, 38
Granada Investments, Inc. v. *DWG Corp.*, 962 F.2d 1203 (6th Cir. 1992)	43, 47
Grant v. *United States*, 227 U.S. 74 (1913)	13
Greenspun v. *Bogan*, 492 F.2d 375 (1st Cir. 1974)	43
Guion v. *Liverpool, London, & Globe Ins. Co.*, 109 U.S. 173 (1883)	22
Guthrie v. *Evans*, 815 F.2d 626 (11th Cir. 1987)	23, 28, 29, 44, 45
Hanna v. *Plumer*, 380 U.S. 460 (1965)	21
Hansberry v. *Lee*, 311 U.S. 32 (1940)	25, 38, 39, 45
Hawes v. *Oakland*, 104 U.S. 450 (1882)	11, 46
Heilman v. *Ginberg*, 284 F.2d 239 (D.C. Cir. 1960)	20
Hohn v. *United States*, 118 S. Ct. 1969 1998)	1
Hurd v. *Illinois Bell Tel Co.*, 234 F.2d 942 (7th Cir.), *cert. denied*, 352 U.S. 918 (1956)	21
INS v. *Chadha*, 462 U.S. 919 (1983)	1, 21

TABLE OF AUTHORITIES—Continued

	Page
Izumi Seimitsu Kogyo Kabushiki Kaisha v. *U.S. Philips Corp.*, 510 U.S. 27 (1993)	1
Jenkins v. *Missouri*, 967 F.2d 1245 (8th Cir.), *cert. denied sub nom. Clark* v. *Jenkins*, 506 U.S. 1033 (1992)	31
Johnson v. *Manhattan Ry.*, 289 U.S. 479 (1933)	22, 23
Johnson v. *Manhattan Ry.*, 61 F.2d 934 (2d Cir. 1932), *aff'd*, 289 U.S. 479 (1933)	23
Jones v. *Nuclear Pharmacy, Inc.*, 741 F.2d 322 (10th Cir. 1984)	43
Kahn v. *Sullivan*, 594 A.2d 48 (Del. 1991)	5
Karcher v. *May*, 484 U.S. 72 (1987)	1, 22, 31
Keith v. *Volpe*, 118 F.3d 1386 (9th Cir. 1997)	31
Kind v. *Markham*, 7 F.R.D. 265 (S.D.N.Y. 1945)	13
Kneeland v. *American Loan & Trust Co.*, 136 U.S. 89 (1890)	35
Koster v. *(American) Lumbermens Mut. Cas. Co.*, 330 U.S. 518 (1947)	25
Krasner v. *Dreyfus Corp.*, 500 F. Supp. 36 (S.D.N.Y. 1980)	43
Lampf, Pleva, Lipkind, Prupis & Petigrow v. *Gilbertson*, 501 U.S. 350 (1991)	48
Ex parte Leaf Tobacco Bd., 222 U.S. 578 (1911)	13, 22
Lexecon, Inc. v. *Milburg Weiss Bershad Hynes & Lerach*, 118 S. Ct. 956 (1998)	49
Litchfield v. *Goodnow's Adm'r*, 123 U.S. 549 (1887)	24
Lloyd v. *Johnes*, 9 Ves. Jun. 37, 32 Eng. Rep. 514 (Ch. 1804)	38
Loran v. *Furr's/Bishop's Inc.*, 988 F.2d 554 (5th Cir. 1993)	28
Maher v. *Zapata Corp.*, 714 F.2d 436 (5th Cir. 1983)	43, 47
Marek v. *Chesny*, 473 U.S. 1 (1985)	46
Marino v. *Ortiz*, 484 U.S. 301 (1988)	7, *passim*
Markman v. *Westview Instruments, Inc.*, 517 U.S. 370 (1996)	36
Martin v. *Wilks*, 490 U.S. 755 (1989)	48, 49

TABLE OF AUTHORITIES—Continued

	Page
Martindell v. *International Tel. & Tel. Corp.*, 594 F.2d 291 (2d Cir. 1979)	31
Matsushita Elec. Indus. Co. v. *Epstein*, 516 U.S. 367 (1996)	45
McDermott, Inc. v. *AmClyde*, 511 U.S. 202 (1994)	45
McKenna v. *Pan American Pet. Corp.*, 303 F.2d 778 (5th Cir. 1962)	21
McShane v. *United States*, 366 F.2d 286 (9th Cir. 1966)	20
Miller v. *Republic Nat'l Life Ins. Co.*, 559 F.2d 426 (5th Cir. 1977)	43
Mississippi Pub. Co. v. *Murphree*, 326 U.S. 438 (1946)	21
Mitchell v. *Lay*, 48 F.2d 79 (9th Cir. 1930), *cert. denied*, 283 U.S. 864 (1931)	32
New York v. *Reebok Int'l, Ltd.*, 96 F.3d 44 (2d Cir. 1996)	40
In re Oracle Securities Litig., 829 F. Supp. 1176 (N.D. Cal. 1993)	43
Osborne v. *Usher*, 6 Bro. P.C. 20, 2 Eng. Rep. 905 (H.L. 1721)	38
In re Pacific Enterprises Sec. Litig., 47 F.3d 373 (9th Cir. 1995)	43
Pavelic & LeFlore v. *Marvel Entertainment Group*, 493 U.S. 120 (1989)	15
Payne v. *Niles*, 20 How. 219 (1858)	22
Pearson v. *Ecological Science Corp.*, 522 F.2d 171 (5th Cir. 1975), *cert. denied sub nom. Skydell* v. *Ecological Science Corp.*, 425 U.S. 912 (1976)	43
Pease v. *Rathbun-Jones Engineering Co.*, 243 U.S. 273 (1917)	35
Phillips Pet. Co. v. *Shutts*, 472 U.S. 797 (1985)	25, 27, 33, 38
Pianta v. *H.M. Reich Co.*, 77 F.2d 888 (2d Cir. 1935)	26
Pierpont v. *Fowle*, 19 Fed. Cas. 652 (C.C.D. Mass. 1846) (No. 11,152)	36

TABLE OF AUTHORITIES—Continued

	Page
In re Pittsburgh & L.E.R.R. Securities and Antitrust Litig., 543 F.2d 1058 (3d Cir. 1976)	43
Public Serv. Comm'n v. *Philadelphia Rapid Transit Co.*, 82 F.2d 481 (3d Cir. 1935), *cert. denied sub nom. Citizens Passenger Ry.* v. *Public Serv. Comm'n*, 298 U.S. 673 (1936)	13
Rosenbaum v. *MacAllister*, 64 F.3d 1439 (10th Cir. 1995)	28, 43
Ross v. *Bernhard*, 396 U.S. 531 (1970)	11, 25
Sage v. *Railroad Co.*, 96 U.S. 712 (1878)	36
Saylor v. *Bastedo*, 623 F.2d 230 (2d Cir. 1980)	43
Schiavone v. *Fortune*, 477 U.S. 21 (1986)	48
Shlensky v. *Dorsey*, 574 F.2d 131 (3d Cir. 1978)	43
Shults v. *Champion Int'l Corp.*, 35 F.3d 1056 (6th Cir. 1994)	27, 44, 45
Smith v. *Barry*, 502 U.S. 244 (1992)	20
Smith v. *Sperling*, 354 U.S. 91 (1957)	7, 18
In re Southeast Banking Corp. Securities Litig., 51 F.3d 1003 (11th Cir. 1995), *cert. denied sub nom. Brandt* v. *Weiner*, 516 U.S. 1044 (1996)	28, 29
Stacy v. *Thrasher*, 6 How. 44 (1848)	24
TBK Partners, Ltd. v. *Western Union Corp.*, 675 F.2d 456 (2d Cir. 1982)	43
Toledo Scale Co. v. *Computing Scale Co.*, 261 U.S. 399 (1923)	35
Torres v. *Oakland Scavenger Co.*, 487 U.S. 312 (1988)	20, 48
Tryforos v. *Icarian Dev. Co.*, 518 F.2d 1258 (7th Cir. 1975) (Stevens, J.), *cert. denied sub nom. Manta* v. *Tryforos*, 423 U.S. 1091 (1976)	8, 28, 29
United Airlines, Inc. v. *McDonald*, 432 U.S. 385 (1977)	17, 18
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United Founders Life Ins. Co. v. *Consumers Nat'l Life Ins. Co.*, 447 F.2d 647 (7th Cir. 1971)	43
United States v. *Brooks*, 164 F.R.D. 501 (D. Ore. 1995)	13

TABLE OF AUTHORITIES—Continued

	Page
United States v. *Pan American World Airways, Inc.*, 299 F.2d 74 (5th Cir. 1962), *rev'd sub nom. Gondeck* v. *Pan American World Airways, Inc.*, 382 U.S. 25 (1965)	20
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United States ex rel. Louisiana v. *Jack*, 244 U.S. 397 (1917)	22, 24, 25
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United States Catholic Conference v. *Abortion Rights Mobilization*, 487 U.S. 72 (1988)	31
In re VMS Ltd. Partnership Securities Litig., 976 F.2d 362 (7th Cir. 1992)	29
Walker v. *City of Mesquite*, 858 F.2d 1071 (5th Cir. 1988)	28, 44
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Weiser v. *Grace*, No. 106285/95 (Sup. Ct., N.Y. Co., N.Y.)	5
Wesson v. *Mississippi River Corp.*, 486 F.2d 1398 2d Cir. 1973), *cert. denied sub nom. Wesson* v. *Levin*, 414 U.S. 1112 (1973)	43
West v. *Randall*, 29 Fed. Cas. 718 (C.C.D.R.I. 1820) (No. 17,424)	38
Wichita & Affiliated Tribes v. *Hodel*, 788 F.2d 765 (D.C. Cir. 1986)	16
Wiener v. *Roth*, 791 F.2d 661 (8th Cir. 1986)	43
Wilkenson v. *Hercules Engines, Inc.*, 138 F.3d 608 (6th Cir. 1998)	27
Williams v. *Morgan*, 111 U.S. 684 (1884)	34, 35
Wolf v. *Barkes*, 348 F.2d 994 (2d Cir.), *cert. denied sub nom. Wolf* v. *Blair*, 382 U.S. 941 (1965)	31, 45
Wormley v. *Wormley*, 8 Wheat. 421 (1823)	38
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TABLE OF AUTHORITIES—Continued

	Page
Zimmerman v. *Bell*, 800 F.2d 386 (4th Cir. 1986)	43
Constitutional Provisions:	
U.S. Constitution, Art. III	18
Statutes:	
Act of June 6, 1900, ch. 803, 31 Stat. 660	23
Antitrust Procedures and Penalties Act, 88 Stat. 1706 (1974), 15 U.S.C. § 16	41
Comprehensive Environmental Response Compensation and Liability Act, 100 Stat. 1678 (1986), 42 U.S.C. § 9622	41
Judiciary Act of 1789, Act of Sept. 24, 1789, ch. 20, 1 Stat. 73	36
Private Securities Litigation Reform Act of 1995, 109 Stat. 737 (1995), 15 U.S.C. § 78u-4	49
Process Act, Act of May 8, 1792, ch. 36, 1 Stat. 275	36
Securities Litigation Uniform Standards Act of 1998, 112 Stat. 3227 (1998), amending sections following 15 U.S.C. §§ 77 and 78	49
Solid Waste Disposal Act, 98 Stat. 3271, 3273 (1984), 42 U.S.C. § 6973	41
105 Stat. 1076 (1991), 42 U.S.C. § 2000e-2	48
105 Stat. 2387 (1991), 15 U.S.C. § 78aa-1	48
2 U.S.C. § 288e	21
28 U.S.C. § 473	41, 46
28 U.S.C. § 1254	1
28 U.S.C. § 1292	23
28 U.S.C. § 1404	2
28 U.S.C. § 2072	21, 50
28 U.S.C. § 2403	21
28 U.S.C. § 1254 (1982)	1
28 U.S.C. § 227 (1928)	23
Regulations:	
28 C.F.R. § 50.7	41

TABLE OF AUTHORITIES—Continued

Rules: Page

Federal Rules of Appellate Procedure:
- Rule 1 20
- Rule 3 ..... 1, *passim*
- Rule 4 ..... 1, 19, 20
- Rule 15 21

Federal Rules of Civil Procedure:
- Rule 14 19
- Rule 16 46
- Rule 19 19
- Rule 23 ..... 1, *passim*
- Rule 23.1 ..... 1, *passim*
- Rule 24 ..... 1, *passim*
- Rule 25 24
- Rule 26 19
- Rule 32 19
- Rule 34 19
- Rule 37 19
- Rule 60 19
- Rule 68 46
- Former Rule 73 ..... 1, 20, 23

Rules of Practice for the Courts of Equity of the United States:
- Rule 27 (1912) 1, 11
- Rule 37 (1912) 1, 15
- Rule 38 (1912) 1
- Rule 39 (1912) 1
- Rule 94 (1882) 1, 11

Federal Rules of Evidence:
- Rule 408 46

Rules of the Supreme Court of the United States:
- Rule 12.4 19
- Rule 12.6 19
- Rule 18.1 ..... 19, 20
- Rule 18.2 ..... 19, 20

Rules of the United States Courts of Appeals:
- First Circuit Rule 47.5 46
- Second Circuit Rules, App. C 46
- Sixth Circuit Rule 18 46
- Ninth Circuit Rule 33-1 46

TABLE OF AUTHORITIES—Continued

Page

- Tenth Circuit Rule 33.1 46
- Eleventh Circuit Rule 33-1 46
- D.C. Circuit Rules, App. III 46
- Federal Circuit Rule 33 46

Orders:
- 104 U.S. ix (1882) (adopting Federal Equity Rule 94) 11
- 226 U.S. 629, 656 (1912) (adopting Federal Equity Rule 27) 11
- 308 U.S. 649 (1938) (adopting Federal Rules of Civil Procedure) 20
- 383 U.S. 1031, 1050 (1966) (adopting Fed. R. Civ. P. 23.1) 11
- 389 U.S. 1065 (1967) (adopting Federal Rules of Appellate Procedure) 20
- 507 U.S. 1061, 1063 (1993) (amending Fed. R. App. P. 3) 48
- 507 U.S. 1091 (1993) (amending Federal Rules of Civil Procedure) 50
- 118 S. Ct. pref. 399 (1988) (amending Fed. R. Civ. P. 23 and Fed. R. App. P. 3) 50

Bills:
- H.R. 660, 105th Cong. 49
- H.R. 1252, 105th Cong. 49
- H.R. 1283, 105th Cong. 49
- H.R. 1689, 105th Cong. 49
- H.R. 3789, 105th Cong. 49
- S. 2083, 105th Cong. 49

Miscellaneous:
- ADMINISTRATIVE OFFICE OF THE UNITED STATES COURTS, STATISTICAL TABLES FOR THE FEDERAL JUDICIARY, DECEMBER 31, 1997, Table X-5 (1998) 40
- Advisory Committee Notes, 39 F.R.D. 69 (1966) 14, 16, 39
- Advisory Committee Notes, 43 F.R.D. 119 (1967) 20
- Advisory Committee Notes, 56 F.R.D. 187 (1972) 46

TABLE OF AUTHORITIES—Continued

Page

Advisory Committee Notes, 113 S. Ct. pref. 473 (1992) 48

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TABLE OF AUTHORITIES—Continued

Page

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JURISDICTION

Title 28 U.S.C. § 1254(1), which is invoked for this Court's jurisdiction, Pet. Cert. 1, authorizes review of cases in the courts of appeals by certiorari "granted upon the petition of any party to any civil or criminal case." CalPERS and FSBA describe themselves as "parties to the proceedings in the court of appeals." Pet. Br. ii.

This Court has said that "[o]ne who has been denied the right to intervene in a case in a court of appeals may petition for certiorari to review that ruling." *Izumi Seimitsu Kogyo Kabushiki Kaisha* v. *U.S. Philips Corp.*, 510 U.S. 27, 30 (1993); *cf. Hohn* v. *United States*, 118 S. Ct. 1969, 1975-76 (1998). CalPERS and FSBA, however, specifically claimed a right to appeal as non-parties, J.A. 349, did not seek to intervene in the Court of Appeals, and were not appealing a denial of intervention by the district court. Hence, unlike cases in which a petitioner has sought and been denied intervention, in this unusual case jurisdiction under § 1254(1) appears to be lacking.[1]

STATUTES AND RULES INVOLVED

Rules 23, 23.1 and 24 and former Rule 73 of the Federal Rules of Civil Procedure, Rules 3 and 4 of the Federal Rules of Appellate Procedure, 28 U.S.C. § 1254, former 28 U.S.C. § 1254, and former Federal Equity Rules 27, 37, 38, and 39 (1912) and 94 (1882) are reproduced at pages 1a-19a, *infra*.

STATEMENT

A. Proceedings in the District Court.

1. *The Complaints.*—These are two derivative actions filed in 1995 by shareholders of Archer Daniels Midland

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[1] *Cf. INS* v. *Chadha*, 462 U.S. 919, 930 n.5 (1983) (noting that petitioners had been granted post-judgment intervention by court of appeals and "are therefore proper 'parties' within the meaning of that term in 28 U. S. C. § 1254(1)"); *Karcher* v. *May*, 484 U.S. 72, 81 (1987) (dismissing under parallel provision of former 28 U.S.C. § 1254(2)).

Company (ADM), consolidated and transferred to the United States District Court for the Central District of Illinois. The defendants were directors of ADM allegedly responsible for losses from antitrust violations, and ADM itself. J.A. 34, 43. Fourteen other shareholder derivative actions were filed in Delaware, the state of ADM's incorporation.[2] An initial consolidated complaint was dismissed with leave to amend, J.A. 14, 201, after which an amended complaint with supplements was filed. J.A. 56, 95, 98. It sought money damages against the directors on behalf of the company, and unspecified equitable relief. J.A. 91-92. Another motion to dismiss was filed and briefed. J.A. 93.

2. *The Proposed Settlement.*—In May 1997 after six months of negotiations counsel for the plaintiff shareholders in Illinois and Delaware, counsel for the defendant directors, and counsel for ADM reached a proposed settlement of all sixteen cases. J.A. 108, 111, 207-08, 211, 328. It called for payment by the directors to ADM of $8,000,000, J.A. 207, 213, 216-17, of which at least $4,080,000 would be made available for funding a compliance program in which independent outside counsel would assist a new ADM Audit Committee, and up to $3,920,000 would pay attorneys' fees and litigation expenses of the shareholders both in Illinois and Delaware. J.A. 118, 120, 196. ADM also agreed to restructuring of its board of directors, and permanently to adopt extensive procedures to increase director independence and safeguard against illegal conduct. J.A. 112, 128-33, 186-88, 190, 212-13, 261-62. The proposal further specified that it did not settle the corporation's claims against former board member Michael Andreas and five other ADM

[2] The Illinois cases were *Felzen* v. *Andreas, et al.*, No. 95 C 4006 (N.D. Ill.); *Esner* v. *Andreas, et al.*, No. 95 CH 6623 (Cir. Ct., Cook Co., Ill.), removed, both transferred pursuant to 28 U.S.C. § 1404(a). The Delaware cases were consolidated as *In re Archer Daniels Midland Co. Derivative Litig.*, No. 14403 (Chan. Ct., New Castle Co., Del.), see J.A. 108-09, 160, and are stayed pending this Court's decision.

employees, a group that included the only individuals charged with and subsequently convicted of antitrust violations. J.A. 115, 120-23, 138, 213, 215.[3] The Illinois plaintiffs agreed that upon final approval of the settlement all their cases would be dismissed with prejudice, J.A. 123, and the Delaware plaintiffs agreed that upon the judgment in Illinois becoming final and unappealable, the Delaware cases would be dismissed as well, J.A. 115-16, 123, 142. A reconstituted ADM board with new membership approved the settlement. J.A. 111; see J.A. 207, 210, 280.

Pursuant to Rule 23.1, Fed. R. Civ. P., the District Court entered an order preliminarily approving the settlement, ordering that notice be sent to all ADM shareholders, and scheduling a fairness hearing to be held five weeks later at which any shareholders who submitted objections would be heard. J.A. 121-22, 134, 139-40, 143-45, 146. More than 243,000 notices were mailed to ADM's shareholders. J.A. 158, 197, 213, 344. Each notice stated that it was "merely to advise you of the pendency and proposed Settlement of the Derivative Claims and of your rights thereunder." J.A. 135. It explained that any shareholder "may appear at the Settlement Hearing to show cause why the proposed Settlement should not be approved." J.A. 140.

3. *Objections.*—Approximately a month after the notice, objections were submitted to the District Court by two large institutional shareholders: the California Public Employees' Retirement System (CalPERS) and the Florida State Board of Administration (FSBA), petitioners here. J.A. 296. CalPERS and FSBA are large state-employee pension funds. CalPERS is the largest governmental pension fund in the United States, with assets

[3] The plaintiffs' attorneys declared that "[t]here has been no evidence that any director of ADM, other than Michael Andreas, was aware of any price-fixing activities, or that the ADM Board systematically failed to exercise its oversight responsibilities." J.A. 205.

exceeding $110 billion; FSBA's assets exceed $83 billion. J.A. 297. Together they own more than 4.5 million shares of ADM's common stock. J.A. 297-98, 335.[4] CalPERS and FSBA had proposed revisions of the organization and procedures by which ADM's board of directors operated, and of its definition of independence. In 1996 these had been defeated by majority vote of ADM's shareholders. J.A. 308, 318-19. For several months prior to the settlement proposal, counsel for the Illinois plaintiffs had discussed the litigation and possible settlement terms with CalPERS, with other institutional shareholders, and with the staff of the Council of Institutional Investors (CII), an association of large pension funds of which CalPERS and FSBA are two of the largest members. J.A. 208-09, 298, 312-13, 316, 318, 328-31.

Affidavits of academic and financial experts concluded that "the Settlement confers significant corporate governance benefits," J.A. 191, and that the settlement "will move ADM to the very forefront of American corporations in terms of corporate governance," J.A. 281. As Professor John C. Coffee, Jr. of Columbia University, who had consulted in the settlement, explained: "In general, I believe the Corporate Governance Provisions [of the settlement] represent more or less the 'state of the art' in American corporate governance today," with "virtually every reform about whose desirability there today exists a significant consensus." J.A. 226.

CalPERS and FSBA informed the District Court that they disagreed with the settlement because, although making permanent the director-independence requirements and other governance changes that ADM had adopted, as well as additional ones, it still did not provide all that CalPERS and FSBA desired. They argued that the settlement instead should have adopted the definition of director independence and all the governance changes they had sought in their proposal that the shareholders of ADM the preceding year had defeated. J.A. 308, 316, 320. An affidavit of a CII staff member said that "ADM has been a poster child for the corporate governance movement for years" and that "[t]his opportunity should not be squandered." J.A. 314. CalPERS and FSBA dismissed the analyses supporting the settlement as the work of "hired experts." J.A. 310. They also objected to the amount of attorneys' fees. J.A. 302.

[4] ADM has over 530 million shares of common stock outstanding, J.A. 337, of which the holdings of CalPERS and FSBA together represent less than 1%. See J.A. 343. ADM has 367 shareholders classified as institutional investors. J.A. 343.

At no time did CalPERS and FSBA move pursuant to Fed. R. Civ. P. 24 to intervene. Counsel for the shareholder plaintiffs pointed out at the hearing that CalPERS on other occasions had moved to make itself a party in derivative actions, and "They know how to do it when they want to, judge." J.A. 338.[5]

4. *The Fairness Hearing.*—CalPERS and FSBA never contended that the plaintiff shareholders were not adequate representatives. CalPERS and FSBA did tell the District Court that in general "derivative actions ha[ve] a unique potential for collusion" and "[w]e think that is what has happened here." J.A. 339-40; see also J.A. 300, 305. When challenged by the District Court to support the epithet "collusion," CalPERS and FSBA responded that "[w]rongdoing [is] . . . in the eyes of the beholder," J.A. 341, and "I make no assertion of any impropriety, Your Honor," J.A. 338.

After hearing arguments from the parties, from CalPERS and FSBA, and from another objector appearing *pro se*,[6] the District Court concluded:

[5] He cited *Weiser* v. *Grace*, No. 106285/95, Sup. Ct., N.Y. County, N.Y. (CalPERS motion to intervene to become representative plaintiff); *cf. Kahn* v. *Sullivan*, 594 A.2d 48, 50 (Del. 1991) (intervention by CalPERS).

[6] Five objections in addition to CalPERS' and FSBA's were received from ADM's 243,000 shareholders. See J.A. 150-56, 197, 263.

—That "I find no basis for claims of collusion. Just none." J.A. 347; see also J.A. 346.

—That "[t]he case the plaintiffs had was not, as one of my colleagues described, 'another case as a dead bang winner.' Far from it." J.A. 345. "This case would have gone on for years. . . . [M]y guess would be five years of further litigation." J.A. 346.

—That "the overwhelming reaction to the proposed settlement [by shareholders] has been acceptance." J.A. 347.

—That "the settlement, which is before the court is fair, reasonable, and adequate." J.A. 345.

On July 7, 1997, final judgment was entered approving the settlement and dismissing the Illinois cases with prejudice, P.C.A. 11a, and an order was entered allowing $3,920,000 for the attorneys' fees and expenses of all the law firms that had represented the plaintiffs in the Illinois and Delaware actions. J.A. 219, P.C.A. 16a.

5. *The Notice of Appeal.*—CalPERS and FSBA still did not move to intervene. Instead, on July 14, 1997 they filed a notice of appeal to the United States Court of Appeals for the Seventh Circuit. In it they described themselves as

> "Objectors . . . each of whom is entitled to appeal from the Final Judgment and Order of Dismissal (July 7, 1997), and Order Awarding Attorneys' Fees and Reimbursement of Expenses (July 7, 1997). . . ." J.A. 349.

B. Proceedings in the Court of Appeals.

The shareholder plaintiffs moved to dismiss the appeal on the ground that CalPERS and FSBA could not appeal because they had neither been, nor sought to become, parties in the District Court. J.A. 350. The Court of Appeals (Posner, C.J., and Flaum and Easterbrook, JJ.) agreed, and dismissed the non-party appeal.

In an opinion by Judge Easterbrook, the court quoted this Court's opinion in *Marino* v. *Ortiz*, 484 U.S. 301 (1988), that "The rule that only parties to a lawsuit, or those that properly become parties, may appeal an adverse judgment, is well settled." 484 U.S. at 304, quoted at P.C.A. 1. The Court of Appeals also cited Rule 3(c), Fed. R. App. P., which provides that "A notice of appeal must specify the *party or parties* taking the appeal . . . ." P.C.A. 2a (emphasis by the court). The court also referred to its own previous holding that to allow members of a class who were not named plaintiffs to appeal would be an "affront to intelligent judicial administration." *In re Brand Name Prescription Drugs Antitrust Litig.*, 115 F.3d 456, 457 (7th Cir. 1997).

Noting that *Marino* had rejected appeal by a non-party in a class action under Rule 23, Fed. R. Civ. P., the Court of Appeals explained that in a Rule 23.1 shareholder derivative action, the jurisdictional deficiency of a non-party appeal is even more apparent:

> "Although there are differences between class actions and derivative suits, these cut against the appellants' position. . . . It is the fact that each class member has a real grievance with the defendant that sets up at least an equitable argument for a class member who wants to appeal. But in a shareholders' derivative action, the individual investor is not an injured party and is not entitled to litigate. A derivative suit is brought by an investor in the corporation's (not the investor's) right to recover for injury to the corporation."

P.C.A. 4a-5a. The court pointed out that any damages recovered in a derivative suit go to the corporation, and that the citizenship of derivative-suit plaintiffs is ignored for diversity jurisdiction. *Id.* at 5a, citing *Smith* v. *Sperling*, 354 U.S. 91 (1957). Although "monitoring [of settlements] is often useful and . . . intervention to facilitate an appeal could be justified," that "does not dispense with the need for an appeal by a party." *Id.* at 6a.

The Court of Appeals overruled a pre-*Marino* decision to the contrary,[7] P.C.A. 3a-4a, 7a, and expressed disagreement with a Third Circuit decision that had allowed non-party shareholders to appeal after concluding that they had "standing." *Bell Atlantic Corp.* v. *Bolger*, 2 F.3d 1304 (3d Cir. 1993). Standing, the Seventh Circuit said, looks only to injury, and "[p]arties are a subset of injured persons. Equating injury with party status is exactly the approach disapproved by *Marino*." P.C.A. 7a.[8]

CalPERS and FSBA sought certiorari, raising two questions: whether the Court of Appeals' holding that non-parties could not appeal was correct, and whether it should be made prospective only. Pet. Cert. i. This Court, Justice O'Connor not participating, granted certiorari as to the first question only. J.A. 351.

SUMMARY OF ARGUMENT

The issue before this Court is not whether shareholders objecting to a settlement of a derivative action may appeal. Clearly the Federal Rules provide ample means for their doing so. The only issue is whether CalPERS and FSBA may appeal on their own terms—without judicial leave, without the responsibilities of a party, and without complying with the procedure the Federal Rules establish.

For nearly 150 years this Court has held on many occasions that persons may not appeal the judgment of a federal court to which they have not been made or

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[7] *Tryforos* v. *Icarian Dev. Co.*, 518 F.2d 1258 (7th Cir. 1975) (Stevens, J.), *cert. denied sub nom. Manta* v. *Tryforos*, 423 U.S. 1091 (1976), which stated in a footnote that a non-party shareholder could appeal provided he or she had appeared in the district court. 518 F.2d at 1263 n.22. Justice Stevens later joined this Court's unanimous opinion in *Marino*.

[8] The Court of Appeals also held, citing *Firestone Tire & Rubber Co.* v. *Risjord*, 449 U.S. 368, 379 (1981), and similar decisions of this Court, that its jurisdictional ruling could not be made prospective only. P.C.A. 7a.

sought to become a party. Ten years ago this Court reiterated that familiar rule in the context of non-parties who objected to a class-action settlement and then attempted to appeal. *Marino* v. *Ortiz*, 484 U.S. 301 (1988).

CalPERS and FSBA argue that the rule, already "well settled" in 1850, should not apply to shareholders who submitted and argued objections to the settlement of a derivative action under Fed. R. Civ. P. 23.1. As legal analogy, they rely on cases in which persons became parties without intervention, as by order of a court, or by submitting to jurisdiction in an ancillary proceeding. As an excuse for not complying with the procedure specified in Fed. R. Civ. P. 24 for intervention, they and *amici* say that being large institutions they have difficulty reaching decisions promptly, and that they do not wish to bear the costs or obligations of parties. As incentive to grant the result they seek, they argue that some settlements of derivative actions are unwise or collusive, so that permitting more persons to appeal to block settlements would be a good thing.

There exists, however, written law that governs who may appeal the judgment in a civil action. With respect to settlements of derivative actions, Fed. R. Civ. P. 23.1 provides only that shareholders must be notified of a proposed settlement, and district-court approval must be obtained. Rule 23.1 does not convert objectors into parties—a distinction that was clear in the minds of its drafters—nor confer on them a right of appeal. The method to seek the status of a party is prescribed in Fed. R. Civ. P. 24, which requires a motion, a showing, and judicial determination. In addition, Rule 3(c) of the Federal Rules of Appellate Procedure in terms reserves the right of appeal to parties—as was held not only by this Court in *Marino*, but in many prior cases interpreting the identical language in Rule 3(c)'s predecessor. The Rules did not prevent CalPERS and FSBA from becoming parties—if they had moved to do so. But they did not want to be parties. They wanted instead something the Rules do not allow—

to avoid party responsibilities and yet become litigants in the court of appeals, entirely on their own prerogative, simply by filing a notice of appeal.

CalPERS and FSBA now call themselves *de facto* parties, even though neither the District Court nor the parties ever treated them as such. They also try to liken themselves to persons who have acquired the status of parties in ways other than intervention, often unwillingly—those to whom a court has directed a contempt citation or injunction, or who were litigants in ancillary proceedings like execution sales, or attorneys claiming a right to fees. Such situations are plainly unlike that of someone who was given a district court's ear, but who shunned assuming the responsibilities of a party.

The core of CalPERS' and FSBA's argument is to urge what they see as a policy improvement. They believe that it would be healthy to have more appeals of derivative-action settlements. Therefore, they argue, the Federal Rules should be interpreted to allow even non-parties to file such appeals. There is not, they say, "*any* countervailing benefit," Pet. Br. 12 (emphasis theirs), in restricting such appeals to parties.

Surely that is not so. The first countervailing benefit, of course, is faithfulness to the text and historical understanding of the Rules themselves, Rules which embody policy judgments already taken. Secondly, as the government's *amicus* brief with trepidation recognizes, the creature of non-party appeals once loosed would not be easily cabined. The same language that would have to be reread to permit non-party appeals in derivative actions would also govern other litigation, including class actions; in class actions, in fact, class members unlike shareholders in a derivative suit have personal claims at stake. Finally, surely there is something to be said for encouraging settlements; for not opening the courts of appeals to litigants (here very large and sophisticated ones) who spurned the opportunity to become parties but want the benefits; and for continuing, as the Rules prescribe, to vest in courts

some control over who may come from the sidelines to demand that the game be replayed.

Most importantly, whether these two institutional investors have an enlightened policy idea is not the point. Even if their controversial plan were wise, they have come to the wrong forum. Congress twice has recently changed procedures for securities litigation. It could do so again. So could the Rules Advisory Committees, who often recommend changes to this Court. But not a word in the Rules supports the ruling sought here. Whether or not they may some day be changed, revising them is not this Court's task today.

ARGUMENT

I. THE FEDERAL RULES DO NOT AUTHORIZE APPEALS BY NON-PARTIES IN SHAREHOLDER DERIVATIVE ACTIONS.

A. Civil Rule 23.1 Specifies the Procedural Rights of Non-Party Shareholders.

Rule 23.1 of the Federal Rules of Civil Procedure establishes the procedure for "a derivative action brought by one or more shareholders . . . to enforce a right of a corporation . . . , the corporation . . . having failed to enforce a right which may properly be asserted by it." Until the Rule's adoption in 1966, 383 U.S. 1031, 1050, shareholder derivative actions had proceeded under Rule 23, which covers class actions.[9] Rule 23.1 provides that "[t]he derivative action may not be maintained if it appears that the plaintiff does not fairly and adequately represent the interests of the shareholders or members similarly situated in enforcing the right of the corporation

[9] Rule 23.1 was derived from Rule 23, which in turn is traced to Federal Equity Rule 27, 226 U.S. 629, 656 (1912), and its predecessor, Federal Equity Rule 94, 104 U.S. ix (1882), which codified the requirements for shareholder derivative suits in *Hawes* v. *Oakland*, 104 U.S. 450, 461 (1882). See *Daily Income Fund, Inc.* v. *Fox*, 464 U.S. 523, 530-31 n.5 (1984); *Ross* v. *Bernhard*, 396 U.S. 531, 534 n.4 (1970).

or association." *Id.* It also specifies a procedure to be followed in settlements:

> "The action shall not be dismissed or compromised without the approval of the court, and notice of the proposed dismissal or compromise shall be given to shareholders or members in such manner as the court directs."

Id. Thus with respect to settlements the Rule specifies two—but only two—procedural protections to shareholders who have made no effort to intervene in the case: (1) notice of any proposed settlement; and (2) a requirement for approval by the district court.[10]

CalPERS and FSBA assert that "[p]ursuant to Rule 23.1, absent shareholders have an absolute right to appear and object to a settlement," and that "a right to appeal is a critical component of the Rule 23.1 right to object, and a necessary counterpart to Rule 23.1's recognition of the shareholders as *de facto* parties." Pet. Br. 15. But Rule 23.1 nowhere designates non-party shareholders as *de facto* parties; the textual requirement of notice does not come even close to doing so. In addition to what Rule 23.1 commands, the District Court provided an opportunity to submit objections as well as a hearing at which objectors were allowed to and did appear and argue. J.A. 148, 333-47. Nothing in the text of Rule 23.1 converts shareholders, even objecting ones, into parties. And nothing in the Rule remotely hints at conferring on non-party objectors a right that parties enjoy, the right of appeal. Rule 23.1 provides what it provides, and nothing more.

The difference between persons who merely are heard by a court, and persons who become parties through summons or intervention, is elementary. Those who helped draft the original Federal Rules understood very well that distinction, as well as its consequences with respect to appeal:

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[10] By contrast, Rule 23(c) provides that all members of a class under Rule 23(b)(3) be given personal notice if practicable of their right to opt out, and that they may appear through counsel.

> "It must be remembered that the right to be heard is not the same as intervention. . . . One who is only given a right to be heard, and has not intervened, has no right of appeal."

Levi & Moore, *Federal Intervention: II. The Procedure, Status, and Federal Jurisdictional Requirements*, 47 YALE L.J. 898, 938 (1938). The distinction was and is recognized in many contexts. For example, in a reorganization proceeding, " 'If the court below wanted to hear [a non-party objector] as adviser, controller, or representative, it could do so, but this privilege did not give him the right to appeal as a party from the decree of the court,' " and "in this respect intervention finds its chief distinguishing feature from the practice of allowing a party to appear as an *amicus curiae*." *Id.* at 939, quoting *Public Serv. Comm'n* v. *Philadelphia Rapid Transit Co.*, 82 F.2d 481, 487 (3d Cir. (1935), *cert. denied*, 298 U.S. 673 (1936).[11] And in a criminal proceeding then Justice Hughes had written for this Court that "Neither Burlingame's appearance before the court, nor the order of reference, made Burlingame a party to the proceeding . . . . Burlingame had no standing to sue out a writ of error." *Grant* v. *United States*, 227 U.S. 74, 79 (1913). Professor Moore, who had played a large role in drafting the original Rule 23, published the first treatise on the new Federal Rules. In it he was unambiguous about what the Rules provided with respect to appeals:

> "Only a person who has become a party in the court below and who is aggrieved by the judgment or order can appeal therefrom. One who has become a party

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[11] See, *e.g.*, *United States* v. *Brooks*, 164 F.R.D. 501, 507 (D. Ore. 1995) (denying intervention but allowing appearance as *amicus curiae*); *Kind* v. *Markham*, 7 F.R.D. 265, 267 (S.D.N.Y. 1945) (same). *Cf. Ex parte Leaf Tobacco Bd.*, 222 U.S. 578, 580 (1911), in which attorney Benjamin N. Cardozo had argued for mandamus to allow his client to intervene, because "[t]here can be no appeal, because the petitioner was not a party to the suit." This Court often invites the United States or a state to express its views in a case and sometimes allows oral argument; that does not convert either into a party.

> by intervention, substitution, or third-party practice, is within such class."

3 J. MOORE & J. FRIEDMAN, MOORE'S FEDERAL PRACTICE 3393 (1938).

When Rule 23.1 was adopted in 1966, then Professor Benjamin Kaplan, Reporter to the Advisory Committee on Civil Rules, explicitly confirmed the continuing distinction between receiving notice or being heard, and being a party. Explaining Fed. R. Civ. P. 23(c)(2)(C), by which a class member not only was entitled to notice but "may, if the member desires, enter an appearance through counsel," he pointed out that even entering such an appearance does not transform a person into a party:

> "If 'appearance' is read as enabling the class member to be admitted automatically into the action as a party, it would stand in odd contrast to intervention in the action under rule 24, which is not automatic and requires a showing."

Kaplan, *Continuing Work of the Civil Committee: 1966 Amendments of the Federal Rules of Civil Procedure (I)*, 81 HARV. L. REV. 356, 392 n.137 (1967). "[A]ppearance" in Rule 23, he explained, meant a right to receive papers "with a view to deciding, *e.g.*, whether he should move to intervene." *Id.* Certainly no hint appears in the Advisory Committee Notes that by the requirement of notice of a proposed settlement, non-party shareholders might be converted into parties. The Advisory Committee's explanation mentioned nothing more than the district court's power to "require that any appropriate notice be given to shareholders." 39 F.R.D. 69, 108 (1966). Nor was any such intention expressed for the essentially identical language of Rule 23(e), which likewise was added in 1966, requiring notice of settlements of class actions. See *id.* at 107.

CalPERS and FSBA cling to an assertion: "The ability of a shareholder to appeal is coterminous with his ability to object in district court." Pet. Br. 11. But the text of Rule 23.1 suggests no such thing. And clearly the drafters of both Rule 23 and Rule 23.1 believed just the opposite. Assertion is all it is.

A Federal Rule is "as binding as any statute duly enacted by Congress, and federal courts have no more discretion to disregard the Rule's mandate than they do to disregard constitutional or statutory provisions." *Bank of Nova Scotia* v. *United States*, 487 U.S. 250, 255 (1988). See also *Pavelic & LeFlore* v. *Marvel Entertainment Group*, 493 U.S. 120, 123, 126 (1989) ("We give the Federal Rules of Civil Procedure their plain meaning" and "[o]ur task is to apply the text, not to improve upon it"); *Business Guides, Inc.* v. *Chromatic Communications Enterprises, Inc.*, 498 U.S. 533, 540 (1991); *Eisen* v. *Carlisle & Jacquelin*, 417 U.S. 156, 176 (1974); *Chambers* v. *NASCO, Inc.*, 501 U.S. 32, 69 (1991) (Kennedy, J., dissenting) ("[w]e are bound . . . by the Rules themselves"). Just last year this Court reminded:

> "Federal Rules take effect after an extensive deliberative process invoking many reviewers . . . . The text of a rule thus proposed and reviewed limits judicial inventiveness. Courts are not free to amend a rule outside the process Congress ordered . . . ."

Amchem Prods., Inc. v. *Windsor*, 117 S. Ct. 2231, 2248 (1997).

B. Civil Rule 24 Prescribes the Procedure and Standards for Intervention.

Rule 24 of the Federal Rules of Civil Procedure exists for the precise purpose of defining and controlling what persons may add themselves as parties to a lawsuit, and how. Derived from Federal Equity Rule 37, Rule 24 established a more regularized procedure and standards for intervention and determination of party status than had existed before. Under Rule 24, one who wishes to acquire the rights of a party must move to intervene. The Rule specifies standards for intervention, whether as of right (Rule 24(a)) or in the discretion of the district court (Rule 24(b)). It also specifies a procedure that

must be followed, and for judicial determination of the motion (Rule 24(c)). The Rule was amended in 1966 to make clear that one of its purposes was to permit intervention by class members. See Advisory Committee Note, 39 F.R.D. 69, 110-11 (1966).

Professor Kaplan, Reporter of the Advisory Committee, confirmed in 1966 that the redrafters of Rule 24, like the original drafters, precisely recognized that a person who chooses not to intervene cannot later appeal from the judgment in the case:

> "New rule 24(a)(2) invites us to see that the practical consequence to the applicants of being denied intervention is that *they cannot stop a settlement nor*, if dissatisfied with the decree entered after contest, *press their contentions on appeal* . . . ."

Kaplan, *supra*, 81 HARV. L. REV at 405 (emphasis supplied, referring to permissive intervention). "Being party to a suit carries with it significant advantages beyond the amicus' opportunities, not the least of which is the ability to appeal an adverse judgment." *Wichita & Affiliated Tribes* v. *Hodel*, 788 F.2d 765, 775 (D.C. Cir. 1986).

CalPERS and FSBA seek the benefits of party status without the burdens. As non-parties, CalPERS and FSBA escaped the obligations that the Federal Rules impose on a party—responsibilities that they did not want to undertake:

> "intervention involves significant burdens—such as drafting the equivalent of a complaint, submitting to the mandatory disclosure requirements of the Federal Rules, and subjecting oneself to depositions, interrogatories, and document requests."

Pet. Br. 12; see also *id.* at 16 ("the burdens associated with formally intervening"); *id.* at 35 ("significant financial disincentives"); *id.* at 36 ("the costs and burdens associated with party status"). Some of those "burdens" might be less if intervention came late in the proceeding, but at the very least the parties would have an opportunity

to respond,[12] make a record, and have the court decide the motion.[13]

Precisely because it is well recognized that the Federal Rules do not authorize non-parties to appeal, persons sometimes seek leave to intervene in the district court even after judgment, in order that they may appeal. This Court has noted with approval "several decisions of the federal courts permitting post-judgment intervention for the purpose of appeal." *United Airlines, Inc.* v. *McDonald*, 432 U.S. 385, 395 (1977) (footnote omitted); *cf. Marino* v. *Ortiz*, 484 U.S. 301, 304 (1988) ("they failed to intervene for purposes of appeal"); *Arizonans for Offi-*

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[12] A response to such a motion might question, for example, whether CalPERS' and FSBA's insistence on adopting CII's ideal model for corporate governance was primarily to benefit ADM or rather to further their own and CII's goals. According to CalPERS, it "has been and remains in the forefront of shareholder activism. In both the national and international marketplace, CalPERS is recognized as a standard-bearer for the corporate governance movement." See http://www.calpers.ca.gov/invest/corpgov. It submitted to the District Court an article that warned: "CEOs who resist pressure for strong governance risk having Calpers or regulatory bureaucrats tell them what kind of board they should have . . . ." J.A. 325.

[13] It has been suggested that institutional investors may want to avoid discovery's "heightened level of scrutiny for the institution." Grundfest & Perino, *The Pentium Papers: A Case Study of Collective Institutional Investor Activism in Litigation*, 38 ARIZ. L. REV. 559, 603 (1996). Also, *amici* Barclays *et al.* calculate that "the probable costs of intervention nearly always exceed the likely benefits." Barclays Br. 12. *Cf.* comment by general counsel of *amicus* State of Wisconsin Investment Board that "a new activism on the part of institutional investors . . . does not involve assuming control of a case as lead plaintiff" because to do so "is not believed to be cost-effective," and citing "relatively inexpensive mechanisms by which they can make their views known to litigants and courts alike . . . . without incurring the costs or exposing themselves to litigation risks inherent in strategies that require formal participation." Johnson, *Deterrence of Corporate Fraud Through Securities Litigation: The Role of Institutional Investors*, 60 LAW & CONTEMP. PROB. 155, 162 (1997), quoting in part Grundfest & Perino, *supra*, 38 ARIZ. L. REV. at 561.

cial English v. *Arizona*, 520 U.S. 43, 56, 66 (1997) (noting court of appeals' reversal of denial of post-judgment intervention, although questioning Article III standing).[14] If non-parties could appeal without seeking intervention—and without the showing of reasons and standing, the opportunity of the parties to oppose, and the district-court evaluation that Rule 24 prescribes—then the intervention procedure this Court has approved would be pointless.

Compliance with Rule 24 does not keep any person entitled to be a party from reaching the court of appeals. It is well established that if intervention is denied, the denial may be appealed. See *Marino* v. *Ortiz*, *supra*, 484 U.S. at 304; *United Airlines, Inc.* v. *McDonald*, *supra*, 432 U.S. at 393; P.C.A. 3a. Moreover, when denial of intervention is held to have been erroneous, courts of appeals often proceed to the merits of the would-be intervenor's arguments. See *United Airlines*, 432 U.S. at 390.[15]

Nor is compliance with Rule 24 an empty formality. To allow non-parties to confer party status upon themselves, as CalPERS and FSBA attempted to do here, would deprive the parties of any opportunity to object and submit for the record any reasons why such intervention did not satisfy the requirements of the Rule or otherwise should not be permitted. It would impair the control by district courts (and through them courts of

[14] The Court of Appeals observed that "we do not doubt . . . that intervention to facilitate an appeal could be justified." P.C.A. 6a.

[15] One *amicus* argues that some objectors might not be permitted to intervene if to do so would destroy diversity jurisdiction. CII Br. 22. No such impediment existed here, and that it might arise with respect to some objectors on some occasions does not alter the meaning of the Federal Rules. Moreover, the supposition is doubtful. See 7C C. WRIGHT, *et al.*, FEDERAL PRACTICE & PROCEDURE 24 (2d ed. 1986) ("intervention of additional shareholders will not divest a federal court of jurisdiction despite the fact that they are citizens of the same state as defendants"); *cf. Smith* v. *Sperling*, *supra*.

appeals) of the structure and dimensions of federal litigation. CalPERS and FSBA are claiming a power suddenly to convert themselves into litigants by their own will—without any judicial scrutiny, without any opportunity for other parties to object, and without any district-court determination. They would finesse the system and standards commanded in Rule 24, and grant themselves the right of a party to appeal—without any court's approval, simply by filing a notice of appeal.

C. Appellate Rule 3 Specifies That Appeals Are by Parties.

Rule 3 of the Federal Rules of Appellate Procedure reflects the same understanding as the Civil Rules: that to appeal, one must become a party. The text of Rule 3(c), as this Court noted in *Marino* v. *Ortiz*, 484 U.S. 301, 304 (1988), excludes appeals by persons not parties:

> "A notice of appeal must specify the party or parties taking the appeal . . . ."

Fed. R. App. P. 3(c); see also P.C.A. 2a. References confirming that the Appellate Rules require "parties" recur throughout Rule 3(c), and as well in Rules 3(b) and 3(d) and Rule 4(a), and throughout the Federal Rules.[16] Although CalPERS and FSBA argue that "[t]he title of that rule [3(c)] makes plain that it is concerned only with the formal 'content[s] of the notice of appeal,'" Pet. Br. 12, this Court and other courts have held otherwise. See *Marino* v. *Ortiz*, *supra*, 484 U.S. at 304; *Smith*

[16] Who is, and who is not, a party is fundamental to the structure of the Federal Rules. See, *e.g.*, Fed. R. Civ. P. 14(a) (authorizing third-party complaint against "a person not a party"); 19 (determining when a "person" is to be "made a party"); 26(a) (party's disclosure obligations); 32(a) (distinguishing party and non-party depositions); 34 (distinguishing party and non-party document production); 37(a)(1) (different venues for motions to compel discovery from parties or non-parties); 60(b) (party may move to set aside judgment). See also this Court's Rules 12.4, 12.6, 18.1, 18.2 (defining and stating duties of "parties" in Supreme Court).

v. *Barry*, 502 U.S. 244, 248 (1992) ("Rule 3's dictates are jurisdictional in nature"); *Torres* v. *Oakland Scavenger Co.*, 487 U.S. 312, 318 (1988) ("construing Rule 3(c) as a jurisdictional prerequisite").[17]

The pertinent language of Rule 3(c), adopted in 1967, 389 U.S. 1065, 1070, is substantially identical to that of former Fed. R. Civ. P. 73(b), adopted in 1938.[18] Many decisions had held that Rule 73(b) limited appeals to persons who had been parties in the district court. *E.g.*, *McShane* v. *United States*, 366 F.2d 286, 288 (9th Cir. 1966) ("One cannot be an appellant here unless he has been a party in the court below"); *United States* v. *Pan American World Airways, Inc.*, 299 F.2d 74, 76 (5th Cir. 1962) (dismissing appeal of United States because "[i]t was not a party to the proceedings in the district court"), *rev'd on other grounds*, 382 U.S. 25 (1965); *Heilman* v. *Ginberg*, 284 F.2d 239, 240 (D.C. Cir. 1960) (Burger, J.) ("[s]ince appellant was not a party . . . he had no right to appeal").[19]

A non-party may file a motion to intervene in the court of appeals, and on rare occasions these have been

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17 See also *Brotherhood of R.R. Trainmen* v. *Baltimore & O.R.R.*, 331 U.S. 519, 528-29 (1947), referring to "the wise rule that the title of a statute and the heading of a section cannot limit the plain meaning of the text."

18 308 U.S. 649, 749 (1938). Fed. R. Civ. P. 73(b) provided: "The notice of appeal shall specify the parties taking the appeal . . . ." See Advisory Committee Note, 43 F.R.D. 119, 126 (1967) (Rules 3 and 4 "merely restate, in modified form, provisions now found in the civil and criminal rules"). *Cf.* this Court's Rules 18.1 ("The notice of appeal shall specify the parties taking the appeal"), 18.2 ("All parties to the proceeding in the district court are deemed parties entitled to file documents in this Court").

19 *Accord, e.g., Commanding Officer* v. *United States ex rel. Bumanis*, 207 F.2d 499, 501 (6th Cir. 1953); *First Iowa Hydro Elec. Coop.* v. *Iowa-Illinois Gas & Elec. Co.*, 245 F.2d 630 (8th Cir. 1957). Rule 3(c) made no change in those jurisdictional rulings, consistently with Fed. R. App. P. 1(b).

granted.[20] But CalPERS and FSBA never filed such a motion.[21]

II. REJECTION OF NON-PARTY APPEALS LONG PRECEDED THE FEDERAL RULES.

A. *Marino* v. *Ortiz* Confirmed More Than a Century of This Court's Decisions.

In *Marino* v. *Ortiz*, 484 U.S. 301 (1988), affirming a holding of the Second Circuit that non-parties could not

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20 See, *e.g.*, *McKenna* v. *Pan American Pet. Corp.*, 303 F.2d 778, 779 (5th Cir. 1962) ("A court of appeals may, but only in an exceptional case for imperative reasons, permit intervention where none was sought in the district court"); *Baker* v. *Wade*, 769 F.2d 289, 291-92 (5th Cir. 1985) (*en banc*) (9-7), *cert. denied*, 478 U.S. 1022 (1986); *Hurd* v. *Illinois Bell Tel. Co.*, 234 F.2d 942, 944 (7th Cir.), *cert. denied*, 352 U.S. 918 (1956); *United States Cas. Co.* v. *Taylor*, 64 F.2d 521, 526 (4th Cir.), *cert. denied*, 290 U.S. 639 (1933). *Cf. INS* v. *Chadha*, 462 U.S. 919, 930 n.5 (1983) (court of appeals granted intervention after Senate and House passed authorizing resolutions); 28 U.S.C. § 2403 (allowing federal and state governments to intervene in certain constitutional cases and "have all the rights of a party and be subject to all liabilities of a party as to court costs"); 2 U.S.C. § 288e (authorizing Senate Legal Counsel to intervene in certain cases); see also Fed. R. App. P. 15(d) (authorizing intervention in cases reviewing administrative decisions).

21 An *amicus* brief argues that state practice should control an appeal to a United States Court of Appeals. Hamermesh Br. 3-15, 21-25. But "[i]t is settled that if the Rule in point is consonant with the Rules Enabling Act, 28 U.S.C. § 2072, and the Constitution, the Federal Rule applies regardless of contrary state law." *Gasperini* v. *Center for Humanities, Inc.*, 518 U.S. 415, 427 n.7 (1996). See also *Burlington N.R.R.* v. *Woods*, 480 U.S. 1, 8 (1987); *Hanna* v. *Plumer*, 380 U.S. 460, 473 (1965); *Byrd* v. *Blue Ridge Rural Elec. Coop., Inc.*, 356 U.S. 525, 537 (1958). The applicable Federal Rules do not alter the rules of decision governing substantive conduct. See *Mississippi Pub. Co.* v. *Murphree*, 326 U.S. 438, 445-46 (1946). Congress authorized this Court to promulgate federal rules of appellate procedure after being informed by the Judicial Conference that "[u]niformity of procedure in the 11 courts of appeals is today sadly lacking and it is very much in the public interest that uniformity of such procedure be achieved," and concluded that "uniformity of appellate procedure is urgently needed." H.R. Rep. No. 2153, 89th Cong., 2d Sess. 3, 5 (1966).

appeal a class-action consent decree, this Court reminded that "[t]he rule that only parties to a lawsuit, or those that properly become parties, may appeal an adverse judgment, is well settled." 484 U.S. at 304.

Marino was in no sense novel. This Court had reiterated the same rule just a month before, *Karcher* v. *May*, 484 U.S. 72, 77 (1987), and many times previously. The holding long antedates the Federal Rules, and indeed had been called "well settled" more than a century earlier. See *Payne* v. *Niles*, 20 How. 219, 221 (1858) ("it is very well settled in all common-law courts, that no one can bring up, as plaintiff in a writ of error, the judgment of an inferior court to a superior one, unless he was a party to the judgment in the court below . . . ."); *Bayard* v. *Lombard*, 9 How. 530, 551 (1850) ("It is a well settled maxim of the law, that 'no person can bring a writ of error to reverse a judgment who is not a party or privy to the record' "). *Accord, e.g., United States ex rel. Louisiana* v. *Jack*, 244 U.S. 397, 402 (1917) ("a subject no longer open to discussion"); *Ex parte Leaf Tobacco Bd.*, 222 U.S. 578, 581 (1911) ("One who is not a party to a record and judgment is not entitled to appeal therefrom"); *Guion* v. *Liverpool, London, & Globe Ins. Co.*, 109 U.S. 173 (1883) (appeal dismissed when "[h]e had applied for leave to become a party, but this leave was not given"); *Ex parte Cockcroft*, 104 U.S. 578, 578-79 (1882) ("Inasmuch, therefore, as the petitioner was not made a party to the suit, either by an express order of the court to that effect, or by being treated as such, his application for an appeal was properly denied"); *Ex parte Cutting*, 94 U.S. 14, 22 (1877) ("Only parties, or those who represent them, can appeal"); *Connor* v. *Peugh's Lessee*, 18 How. 394, 395 (1856) ("No one but a party to the suit can bring a writ of error").[22] Since

[22] The proper procedure to follow in a receivership was the issue in the unusual jurisdictional dispute in *Johnson* v. *Manhattan Ry.*, 289 U.S. 479 (1933). Rather than submit to the jurisdiction of a particular judge, some creditors who challenged his authority to appoint a receiver filed a new action before a different judge, who consolidated the two cases. This Court held that instead of starting a new action, the plaintiffs should have objected in the existing one, and appealed if dissatisfied. 289 U.S. at 495. This allusion assumed that, already parties in one case, they would have appeared as intervenors in the other, as many other claimants already had, done, *cf. id.* at 489. That assumption was confirmed by Judge Learned Hand's prior rejection of their argument that "they could not safely intervene" in the first action. *Johnson* v. *Manhattan Ry.*, 61 F.2d 934, 939 (2d Cir. 1932), *aff'd*, 289 U.S. 479 (1933). This Court also noted that appeals from appointments of receivers were authorized by a special jurisdictional statute, Act of June 6, 1900, ch. 803, 31 Stat. 660, then codified as 28 U.S.C. § 227 (1928), now as amended 28 U.S.C. § 1292(a)(2); the cases it noted in a footnote, 289 U.S. at 495 n.4, were appeals by parties or debtors or creditors making claims or brought into receivership proceedings.

1938 those longstanding decisions have had the additional authority of codification first in Fed. R. Civ. P. 73(b) and then in Fed. R. App. P. 3(c). See *Marino*, 484 U.S. at 304.

The government concedes in footnotes that "the general rule is that one must intervene in order to litigate (including appeal)." G. Br. 19 n.13; see also *id.* at 26-27 n.21 ("the long-standing general rule that only a party or a privy to the record may appeal"). The government argues, however, to adopt a different rule for derivative actions. It urges that *Marino* (and, apparently, the century of cases it reiterated) should be disregarded because in *Marino* the non-parties seeking to appeal were "strangers to the litigation" and "not members of the class." G. Br. 5. But as one court of appeals explained in rejecting that argument, in *Marino*

> "The Supreme Court was referring to officers who had filed objections to the settlement, and whose counsel was allowed to speak at the hearing and argue against the proposed settlement. . . . While they were not unnamed class members, . . . they were objecting to the approval of a settlement of the class action. We agree with *Guthrie* [v. *Evans*, 815 F.2d 626 (11th Cir. 1987)] that *Marino* provides substantial support for holding that unnamed class

> members who object to a settlement must move to intervene, and they will be denied standing to appeal when they have not done so."

Croyden Assocs. v. *Alleco, Inc.*, 969 F.2d 675, 679 (8th Cir. 1992), *cert. denied*, 507 U.S. 908 (1993). As in *Marino*, in the present case the non-parties were persons wholly distinct from the represented entity, the corporation; indeed, they were asserting a position *adverse* to that of the corporation acting through its Board of Directors, the majority of its shareholders, and its court-approved representatives. In such a posture *Marino*, even as narrowly explained by the government, applies.

Nor is there any basis for CalPERS and FSBA to assert that "[o]bjecting shareholders are at least 'privies to the record,'" Pet. Br. 25, in the sense that that term was used in *United States ex rel. Louisiana* v. *Jack*, *supra*, 244 U.S. at 402. The term "privity" referred usually to "mutual or successive relationship to the same rights of property," *Litchfield* v. *Goodnow's Admr.*, 123 U.S. 549, 551 (1887), and most often was used in the context of succession to estates and contract rights. See *Stacy* v. *Thrasher*, 6 How. 44, 58 (1848); *Bigelow* v. *Old Dominion Copper Mining & Smelting Co.*, 225 U.S. 111, 128-29 (1912); *cf.* Fed. R. Civ. P. 25(c) (substitution of parties succeeding to interest). In a derivative action, however, the claim is entirely the corporation's, and is not one to which individual shareholders succeed. As Judge Prettyman explained:

> "It is sometimes said that not only parties to the record, but also their privies, may appeal, and that if the decree affects a person's interests, he may appeal. We have examined all the cases we have found cited to that proposition, and find that they concern the right to intervene and then appeal."

United States v. *Seigel*, 168 F.2d 143, 145 (D.C. Cir. 1948) (footnotes omitted). In the very case petitioners cite, this Court called a state's argument that it could appeal from a settlement by a subordinate public agency "unsubstantial to the point of being frivolous." *Jack*, 244 U.S. at 401.

CalPERS and FSBA assert repeatedly that they were shareholders "whose rights were necessarily being adjudicated in the derivative action." Pet. Br. 10; see also *id.* at 11. That is not so. Members of a class, who have individual claims, have their own rights being adjudicated in the class action. That is why Rule 23, reflecting due process concerns, provides class members an opportunity to opt out or to appear, and for notice at the time of class certification, not just when a settlement is proposed. See Rule 23(c)(2); *cf. Phillips Pet. Co.* v. *Shutts*, 472 U.S. 797, 812 (1985); *Eisen* v. *Carlise & Jacquelin*, *supra*, 417 U.S. at 173-74; *Hansberry* v. *Lee*, 311 U.S. 32 (1940). But in a shareholder derivative action, which is brought "to enforce a right of a corporation," Rule 23.1, shareholders have no legally enforceable personal rights at stake at all. The only represented entity in a derivative suit is the corporation itself, not its shareholders. The net recovery also belongs only to the corporation. *Ross* v. *Bernhard*, 396 U.S. 531, 538 (1970); *Koster* v. *(American) Lumbermens Mut. Cas. Co.*, 330 U.S. 518 (1947).

The government asserts that "Here, the objecting shareholder has a personal stake in the outcome of a derivative action settlement." G. Br. 17-18. That certainly is incorrect as a matter of law, for any recovery belongs to the corporation. The government assumes that "the shareholders necessarily benefit from whatever recovery the corporation may realize on its claims." G. Br. 13. But even that factual assumption is not necessarily valid as a prediction of real-world economic consequences. Empirical study suggests, on the contrary, that for an ongoing enterprise there is little direct correlation at all [23]—which is why corporations and their shareholders often judge it

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[23] See, *e.g.*, Fischel & Bradley, *The Role of Liability Rules and the Derivative Suit in Corporate Law: A Theoretical and Empirical Analysis*, 71 CORN. L. REV. 261, 282 (1986) ("insignificant magnitude of these wealth-effects"); Romano, *The Shareholder Suit: Litigation Without Foundation?*, 7 J.L. ECON. & ORG. 55, 66-68 (1991).

wise and in their economic interest to terminate costly litigation on reasonable terms.[24]

B. Most Courts of Appeals Have Applied the Rule Reiterated in *Marino*.

The overwhelming weight of authority in the Circuits, before *Marino* and even more strongly since, has been to reject attempts by non-parties in representative actions to appeal. Most of the decisions have come in class actions. The government recognizes, G. Br. 6, that the notion that a non-party might be allowed to appeal in a derivative action originated in a 1942 Sixth Circuit decision, *Cohen* v. *Young*, 127 F.2d 721. Even that case, however, did not hold that what CalPERS is seeking here. For in *Cohen* the objecting shareholder had been served with an order to show cause, 127 F.2d at 723; and entirely unlike CalPERS and FSBA, he had "filed a petition to intervene" in the district court, but his "petition to intervene as plaintiff was denied." 127 F.2d at 723, 724. It is a commonplace that denials of motions to intervene are appealable. See p. 18, *supra*. Moreover, *Cohen* v. *Young*, as the Sixth Circuit twice later explained, depended also on the shareholder there having been actually served with an order to show cause, making him "like a defendant who is summoned by process of court," 127 F.2d at 724, quoting *Pianta* v. *H.M. Reich Co.*, 77 F.2d 888, 890 (2d Cir. 1935).

> "In *Cohen*, the appellant had received an order to show cause why the settlement should not be approved. . . . Cohen had no choice but to participate in the proceedings.
>
> "By contrast, Lennon received no such summons. Lennon argues that he was figuratively 'summoned' into court and 'compelled' to appear in that if he did not, it would have prejudiced any subsequent ERISA claim by him . . . . But . . . . It is only when the court affirmatively orders a non-named party to appear that the party has standing to appeal."

Wilkenson v. *Hercules Engines, Inc.*, 138 F.3d 608, 611 (6th Cir. 1998). In another case the Sixth Circuit has explained that "for a non-named class member to have standing to appeal, there must be more than a mere requirement of notice," so "unnamed class members generally lack standing to appeal class settlements." "[A] mere voluntary appearance to state or file objections is an insufficient basis for standing to appeal." *Shults* v. *Champion Int'l Corp.*, 35 F.3d 1056, 1060, 1061 (6th Cir. 1994).[25] At most, *Cohen* stood for the proposition that one who was served with an order to show cause and who unsuccessfully had sought to intervene could appeal without appealing the intervention denial itself—reflecting the common practice of courts to reach the merits of a claim if they conclude that intervention should have been granted. See p. 18, *supra*.

The Third Circuit many years later ignored the limitations of *Cohen* v. *Young*. In a 1971 decision the Third Circuit with little explanation had allowed non-party class members to appeal in a class action. *Ace Heating & Plumbing Co.* v. *Crane Co.*, 453 F.2d 30, 33 (3d Cir. 1971). Then in 1993 it extended that holding to non-parties in a shareholder derivative action as well, based on its judgment that "assuring fair and adequate settlements outweighs concerns that non-intervening objectors will render the representative litigation 'unwieldy.'" *Bell Atlantic Corp.* v. *Bolger*, 2 F.3d 1304, 1310 (3d Cir. 1993). In another derivative action, the Seventh Circuit

[24] The new ADM board agreed to the settlement of this case "in order to limit further expense, inconvenience and distraction, to dispose of burdensome and protracted litigation, and to permit the operation of ADM's business without further expensive litigation and the distraction and diversion of ADM's executive personnel with respect to matters in issue in the Litigation." J.A. 112.

[25] In the present case the notice sent to shareholders specified that it was "merely to advise you" and that shareholders "*may* appear . . . to show cause why the proposed Settlement should not be approved." J.A. 135, 140 (emphasis supplied). They were "not required to do anything." *Phillips Pet. Co.* v. *Shutts*, *supra*, 472 U.S. at 810.

in 1975 in a footnote relied on *Cohen* v. *Young*, while adding that "no such appeal may be taken by a shareholder who has failed to make such an appearance." *Tryforos* v. *Icarian Dev. Co., supra*, 518 F.2d at 1263 n.22 (Stevens, J.), overruled in the present case, P.C.A. 7a.

Far more often than in derivative actions, non-party attempts to appeal have come up in class actions, particularly settlements under Rule 23(e). And most Circuits have emphatically rejected such attempts—citing *Marino* and similar authorities, and also warning of the consequences of allowing non-party appeals:

> "If individual appeals without formal intervention were to be permitted, the class action would break down under the burden of unpredictable and unlimited individual actions."

Gottlieb v. *Wiles*, 11 F.3d 1004, 1009 (10th Cir. 1993).[26] "[C]lass actions could become unmanageable." *Guthrie* v. *Evans*, 815 F.2d 626, 628 (11th Cir. 1987). An "affront to intelligent judicial administration." *In re Brand Name Drugs, supra*, 115 F.3d at 457. The Fifth Circuit was "[p]ersuaded that the reasoning employed by the Eleventh Circuit in *Guthrie* is correct," and also relied on *Marino*. *Walker* v. *City of Mesquite*, 858 F.2d 1071, 1073, 1074 (5th Cir. 1988); *accord*, *Loran* v. *Furr's/Bishop's Inc.*, 988 F.2d 554 (5th Cir. 1993). The Eighth Circuit agreed that "[w]e believe that *Guthrie* and *Walker* are persuasive authority and we see no decision that has pointed to a flaw in their analysis." *Croyden Assocs.* v. *Alleco, Inc., supra*, 969 F.2d at 680. So did the Seventh Circuit. *In re VMS Ltd. Partnership Securities Litig.*, 976 F.2d 362, 366 (7th Cir. 1992) ("[a]s a non-party, the Oversight Committee's participation in the proceedings challenging the sale of the Lynnhaven properties does not confer upon it the right to appeal the resulting order").[27]

[26] In *Rosenbaum* v. *MacAllister*, 64 F.3d 1439 (10th Cir. 1995), the Tenth Circuit emphasized that

> "To allow a nonintervening class member to appeal approval of a settlement would permit one dissident—and there is likely always to be one—to postpone realization of any of the benefits that might otherwise come to the class members and to prevent the defendant from settling its liability."

64 F.3d at 1442. However, it reasoned that appeal of the separate fee award, rather than of the settlement itself, "seems proper" and "would not be nearly as disruptive." *Id. Contra, In re Southeast Banking Corp. Securities Litig.*, 51 F.3d 1003, 1004 (11th Cir. 1995) ("a non-named class member who failed to intervene, lacks standing to appeal the district court's order on attorney's fees"), *cert. denied*, 516 U.S. 1044 (1996).

For the government to say that the Court of Appeals here "departed from a uniform rule in derivative actions that had long been applied in the courts of appeals," G. Br. 5, is scarcely informative. That statement ignores nearly all the pertinent court of appeals decisions, simply because they rejected non-party appeals in class actions—where the non-party's interest is, if anything, stronger. What the government describes as a "uniform rule" turns out to rest on a total of three cases spread over fifty years: one, *Cohen* v. *Young*, which the Sixth Circuit has confined to its facts, which are not present here; another, *Tryforos*, decided pre-*Marino* citing *Cohen*; and *Bell Atlantic*, in which the Third Circuit acknowledged the contrary authorities, but ruled otherwise based on that court's view of desirable policy. Unless class actions are ignored, the "uniform rule" is almost uniformly the other way.

CalPERS and FSBA and the government cite two treatises. But Moore's simply notes a split of authority on whether non-party objectors in class or derivative actions may appeal. 5 J. MOORE, MOORE'S FEDERAL PRACTICE ¶ 23.1.10[3] (D. Coquillette *et al.*, 3d ed. 1998). The Wright & Miller treatise asserts in a single sentence that a non-party shareholder may appeal; but it offers no supporting reasoning[28] and relies solely on a

[27] The Ninth Circuit, however, has said that it will permit non-party appeals when "the equities weigh in favor of hearing the appeal." *EEOC* v. *Pan American World Airways, Inc.*, 897 F.2d 1499, 1504 (9th Cir.), *cert. denied*, 498 U.S. 815 (1990).

[28] As the government in citing Wright & Miller puts it, "[t]hat rule had been reported by influential commentators without any question as to its validity." G. Br. 5-6. However, the government's

district-court case.[29] An unpublished article cited by CalPERS and FSBA, as its title's reference to "conflicting ideologies "suggests, presents a policy argument for "adopting a rule that requires only objections to preserve appellate rights in derivative suits," while at the same time acknowledging that to do so would "make[] settlements more costly and increase[] the likelihood that settlements will be more difficult to finalize." [30]

C. CalPERS and FSBA Did Not Become Parties Without Intervention.

Just as a defendant becomes a party when served with a summons, persons may become parties when they are subjected to the process or orders of a court, or when they are disputants in ancillary proceedings. No such situation exists here, yet CalPERS and FSBA make a Procrustean effort to fit. Lacking support in the English of the Federal Rules, occasionally they flee to Latin.

1. *They Were Not Made Parties De Facto.*

Throughout their brief CalPERS and FSBA refer to themselves as *de facto* parties, sometimes citing Rule 23.1,

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quotation from the second edition of Moore, G. Br. 6 (citing 3B J. MOORE, MOORE'S FEDERAL PRACTICE (2d ed. 1948-96)), has been deleted from the third edition, as noted above. The government cites to Moore's third edition except for this point, where it instead cites to the second. *Compare* G. Br. 13, 14, *with id.* 6.

[29] 7C C. WRIGHT, *et al.*, FEDERAL PRACTICE & PROCEDURE 182 (2d ed. 1986 & Supp. 1998), citing *Webcor Electronics* v. *Whiting*, 101 F.R.D. 461, 465 n.11 (D. Del. 1984). Its current supplement adds only a citation to the Third Circuit decision in *Bell Atlantic Corp.* v. *Bolger*, *supra*, and does not mention the contrary decisions in the Fifth, Sixth, Eighth, Tenth and Eleventh Circuits, nor mention *Marino* v. *Ortiz*. C. WRIGHT, *et al.*, *supra*, 1998 Supp. at 13 n.22.

[30] Kim, *Conflicting Ideologies of Group Litigation: Who May Challenge Settlements in Class Actions and Derivative Suits?*, ms. at 69-70 (copy lodged with Clerk). No analysis was offered to support the assertion in an article appearing in 1969—citing *Cohen* v. *Young*—that non-party objectors could appeal. Haudek, *The Settlement and Dismissal of Stockholders' Actions—Part II: The Settlement*, 23 S.W.L.J. 765, 803 (1969).

which says no such thing. *E.g.*, Pet. Br. 10, 11, 15. Cases do exist in which a would-be intervenor has been treated by the district court and litigants as a party for all purposes, without entry of an order granting intervention. See, *e.g.*, *Martindell* v. *International Tel. & Tel. Corp.*, 594 F.2d 291, 294 (2d Cir. 1979) ("amounted to a *de facto* grant of permissive intervention pursuant to Rule 24(b)"); *Adams* v. *Morton*, 581 F.2d 1314, 1318 (9th Cir. 1978), *cert. denied*, 440 U.S. 958 (1979). Thus this Court in *Karcher* v. *May*, *supra*, referred to the rule that "one who is not a party *or has not been treated as a party* to a judgment has no right of appeal therefrom." 484 U.S. at 77 (emphasis supplied). But the record leaves no doubt that CalPERS and FSBA were never treated as parties by anyone at any time in the District Court—least of all by themselves. See J.A. 349. If they had been, they would have been subject to all the orders of the court and all the responsibilities of parties—burdens, they said, that they were unwilling to assume. *See* p. 16, *supra*. Their repeated invocation of the self-bestowed soubriquet "*de facto* party" is simply a rehashing of their assertion that by objecting, an objector becomes a party who can appeal. Not so under the Federal Rules.[31]

2. *They Were Not Summoned or Ordered.*

One who has had a court order issued against him or her personally of course may appeal. Contempt and injunctions are examples. See, *e.g.*, *United States Catholic Conference* v. *Abortion Rights Mobilization*, 487 U.S. 72, 76 (1988) ("The right of a nonparty to appeal an adjudication of contempt cannot be questioned"); *Keith* v. *Volpe*, 118 F.3d 1386, 1391 n.7 (9th Cir. 1997) (nonparty may appeal when he "was haled into this action by the district court over his objections"); *Jenkins* v. *Missouri*, 967 F.2d 1245, 1247 (8th Cir.) ("a non party

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[31] *Wolf* v. *Barkes*, 348 F.2d 994 (2d Cir.), *cert. denied*, 382 U.S. 941 (1965), which CalPERS and FSBA cite for the proposition that "absent shareholders are *de facto* parties," Pet. Br. 14, says nothing of the sort.

may appeal an injunction that purports to bind the non party"), *cert. denied*, 506 U.S. 1033 (1992); *Mitchell* v. *Lay*, 48 F.2d 79, 85 (9th Cir. 1930) ("brought into court by the process of the court"), *cert. denied*, 283 U.S. 864 (1931); *Cohen* v. *Young*, *supra*.

CalPERS and FSBA were not like persons responding to a contempt citation, or subjected to an injunction—but now they strain to be. Their tinkering with their own Question Presented to this Court betrays anxiety: they now wish to portray themselves as persons "summoned to appear in federal district court." Pet. Br. i.[32] They, along with 243,000 other ADM shareholders, see J.A. 147, 197, received a letter pursuant to Rule 23.1 giving notice of the proposed settlement. It told them that it was "merely to advise you," and that they "may" appear. J.A. 135, 140. On that basis they now say that "the district court had expressly summoned petitioners to participate in this case pursuant to Rule 23.1." Pet. Br. 9. Their Petition for Certiorari was more accurate. It said that "the district court . . . invited" ADM shareholders to

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[32] The question stated in the Petition, which this Court granted certiorari to review, J.A. 351, was

> "Whether a nonparty shareholder *who appears, in response to notice* provided under Federal Rule of Civil Procedure 23.1, to present objections to a proposed dismissal or settlement of a derivative action may appeal an adverse decision even though the shareholder has not been formally made a party to the action."

Pet. Cert. i (emphasis supplied). The revised question stated in the Brief for Petitioners is:

> "Whether a shareholder *who*, pursuant to Federal Rule of Civil Procedure 23.1, *is summoned to appear* in federal district court and present objections to a proposed dismissal or settlement of a derivative action must also intervene pursuant to Federal Rule of Civil Procedure 24 in order to appeal an adverse decision."

Pet. Br. i (emphasis supplied). *Compare* also Pet. Br. 8 (describing the notice as "directing" shareholders "to 'appear and show cause'") (omitting "may" and "merely to advise you"), *with* J.A. 135, 140.

appear and present objections to the proposed settlement. Pet. Cert. 7; see also *id.* ("the court's invitation"). In reality, of course, Rule 23.1 *summons* no one; it provides that "notice of the proposed dismissal or compromise shall be given to shareholders." CalPERS and FSBA "were not haled anywhere." *Phillips Pet. Co.* v. *Shutts*, *supra*, 472 U.S. at 809.

3. *They Were Not Parties in an Ancillary Proceeding.*

Appeals may arise after a case has spawned subsidiary proceedings, usually post-judgment, that are ancillary to the litigation in chief. Disputes in court-ordered foreclosure sales, enforcement of bonds against sureties, and claims by attorneys for statutory fees, are common examples. See, *e.g.*, *Boyle* v. *Zacharie*, 6 Pet. 648, 656 (1832) ("a writ of error will lie" for "an erroneous award of execution, not warranted by the judgment"). The issues in such disputes are not the ones litigated in the original case, and the adversaries usually are different as well.

Fastening onto the fact that appeals may arise from rulings in such proceedings—which the government itself describes as "ancillary," G. Br. 16—the government urges a conspicuous *non sequitur*: it argues that because rulings may be appealed by parties to ancillary proceedings, appeals should also be permitted to nonparty shareholders who object to the final judgment resolving the very case the parties litigated and settled. G. Br. 11, 15. On the basis of such authority—which the government faintly labels "significant support," G. Br. 16—it asks this Court to ignore Rules 23.1 and 24 and complicate modern civil procedure with an amorphous legal category of "quasi parties."

Even the government is forced to concede how narrow and particularized were the cases it cites, "which permitted *limited appeals* in *discrete circumstances* by certain *'quasi parties,'*" G. Br. 8 (emphasis supplied), recognizing, it says, a *"narrow right* of quasi parties to appeal in *limited*

circumstances," *id.* at 11 (emphasis supplied), cases it acknowledges "included *only a narrow range* of appellants," *id.* (emphasis supplied). The array of qualifiers is essential. All the cases it cites (and which CalPERS and FSBA do not) were collateral or ancillary proceedings and matters discrete from the original litigation, in which the persons contesting were effectively involved in their own separate disputes—"quasi parties" being a term used in some of the cases to characterize the distinction.

The government devotes two pages to *Blossom* v. *Milwaukee R.R.*, 1 Wall. 655 (1864), a case which simply recognized that a bidder in a post-decree foreclosure sale who by court order was denied his purchase could appeal. This Court's opinion in that case opened by reaffirming that

> "It is certainly true that he cannot appeal from the original decree of foreclosure, nor from any other order or decree of the court made prior to his bid."

1 Wall. at 655. It then pointed out that the dispute arose entirely in an ancillary proceeding, and explained that

> "after a decree adjudicating certain rights between the parties to a suit, other persons having no previous interest in the litigation may become connected with the case, in the course of the subsequent proceedings, in such a manner as to subject them to the jurisdiction of the court, and render them liable to its orders . . . ."

1 Wall. at 655-56. Such persons, it said—for example, sureties or receivers on writs of attachment—"become *quasi* parties to the proceedings, and subject themselves to the jurisdiction of the court, so that summary judgments may be rendered on their bonds or recognizances." 1 Wall. at 656. By contrast, it was exactly the *refusal* of CalPERS and FSBA to "subject themselves to the jurisdiction of the court" that caused the dismissal of their appeal.

Similarly, in *Williams* v. *Morgan*, 111 U.S. 684 (1884), another post-decree dispute, this Court stated that "the

only question on the merits relates to the compensation which ought to be allowed to the trustees and receivers of a certain railroad mortgage for their services." 111 U.S. 685. Bondholders, who contested the amount, had been allowed as of right to appeal and become what this Court described as "quasi parties," defined as "persons incidentally interested in some branch of a cause [who] *have been allowed to intervene* for the purpose of protecting their interest." 111 U.S. at 698-99 (emphasis supplied).[33] This Court explained that "the right . . . to appeal . . . depends on their right to intervene." *Id.* at 696.

Moreover, what the government chooses to call "the doctrine of quasi parties," G. Br. 11, is scarcely so exalted. The term originated to describe persons not present but represented in a proceeding in equity. On closer examination one discovers that the terms "quasi party" or "quasi parties" have appeared in only four opinions in the entire history of this Court. The most recent was in 1923, and none of them remotely resembled a non-party shareholder appeal in a derivative action.[34] The rediscov-

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[33] The government speculates that in the Nineteenth Century this Court "often used the term 'intervene' in the sense of participation." G. Br. 17 n.11. That is not demonstrated by any of the three cases it cites. What can more accurately be said is that until 1938 "there has been no settled uniform practice in regard to proper procedure on intervention," and that Rule 24 in 1938 regularized the standards and procedure. Levi & Moore, *supra*, 47 YALE L.J. at 903. The government concedes that "the standards for objecting under Rule 23.1 are different from intervention under Rule 24." G. Br. 24.

[34] In addition to *Blossom* v. *Milwaukee R.R.* and *Williams* v. *Morgan*, already discussed, see *Pease* v. *Rathbun-Jones Engineering Co.*, 243 U.S. 273, 279 (1917) ("sureties become quasi parties to the proceedings, and subject themselves to the jurisdiction of the court, so that summary judgment may be rendered on their bonds"); *Toledo Scale Co. v. Computing Scale Co.*, 261 U.S. 399, 427 (1923) (sureties are liable on their bonds as quasi parties). Several of the cases the government lists as "quasi party" decisions never used such a term at all. *E.g.*, *Kneeland* v. *American Loan & Trust Co.*,

ered antique phrase "quasi parties" occurs more times in the brief the government has filed in this case than in all this Court's decisions for the past two centuries.

D. Developments in English Chancery Did Not Alter the Established Rule.

CalPERS and FSBA also cite a Nineteenth Century English writer's comments on developments in English chancery practice, comments which even if relevant[35] are not at all inconsistent with the rule reiterated in *Marino* and its predecessors. Initially English law courts had been generally unwilling to adjudicate the rights of individuals not present, and would simply dismiss for absence of necessary parties. To elide that difficulty, the Court of Chancery from expediency sometimes pretended that absent persons were present, occasionally referring to them as "*Quasi* parties." *See Cockburn* v. *Thompson*, 16 Ves. Jun. 321, 327, 33 Eng. Rep. 1005, 1007 (Ch. 1809). Such instances arose typically in litigation determining the rights of remaindermen to entailed estates, and also occasionally when an adjudication concerned rights of a group too numerous as a practical matter for all to litigate. Such cases became more numerous in the early Nine-

136 U.S. 89 (1890) (called at G. Br. 16 one of "this Court's quasi party cases"); *Sage* v. *Railroad Co.*, 96 U.S. 712 (1878) (described at G. Br. 10 n.4 as involving "quasi parties").

35 English equity practice after American independence was not considered binding precedent, nor of course were commentaries upon it. "[A] check has wisely been provided against the assumption of equity jurisdiction by any new rule in English courts since the Revolution." *Baker* v. *Biddle*, 2 Fed. Cas. 439, 447 (C.C.E.D. Pa. 1831) (No. 764); see also *Pierpont* v. *Fowle*, 19 Fed. Cas. 652, 655 (C.C.D. Mass. 1846) (No. 11,152); *cf. Cathcart* v. *Robinson*, 5 Pet. 264, 280 (1831). Federal equity jurisdiction was established in the first Judiciary Act, Act of Sept. 24, 1789, ch. 20, §§ 11, 15, 16, 1 Stat. 73, 78, 82, and the Process Act, Act of May 8, 1792, ch. 36, § 2, 1 Stat. 275, 276. *Cf. Galloway* v. *United States*, 319 U.S. 372, 392 n.23 (1943) (noting "plastic and developing character" of English procedure); *Markman* v. *Westview Instruments, Inc.*, 517 U.S. 370, 383 (1996) (noting that an English decision was rendered "more than 70 years after the time that concerns us").

teenth Century, when Lord Eldon was Lord Chancellor; as he candidly explained, "the Court does what it can." *Cockburn* v. *Thompson, supra*, 16 Ves. Jun. at 326, 33 Eng. Rep. at 1007; see discussion in *Duke of Bedford* v. *Ellis*, [1901] A.C. 1, 8-11 (H.L.) (Lord Macnaghten). "The English judges had no hesitation in jumping, not only the obstacle of unjoined parties, but also the obstacle of binding them without a day in court." Z. CHAFEE, SOME PROBLEMS OF EQUITY 212-13 (1950).

The latter point was the concern of Frederic Calvert, who in the 1830s and 1840s urged that "every individual *ought*, as it appears to me, to . . . have the power of appealing, whether he has been a suitor . . . or by some other person as his representative." Quoted at Pet. Br. 20 (emphasis supplied).[36] As the word "ought" signals, Calvert was making proposals for changes in the law. And the background of his suggestion, as was stated in his more substantial treatise, was that "the persons, whom it is proposed to affect by the decree compulsorily, must be made parties on record."[37] He did quote a ruling by the House of Lords that a tenant in tail whose remainder rights had been adjudicated might appeal—but also that the manner to do so was by what today would be called post-judgment intervention: "making himself a party to the suit instituted in said Court, by filing a supplemental Bill to have the benefit of the proceedings therein, for the purpose of

36 F. CALVERT, OBSERVATIONS UPON SOME OF THE DIFFICULTIES ATTENDING SUITS IN EQUITY AMONGST THE SHAREHOLDERS OF JOINT STOCK COMPANIES: With SUGGESTIONS FOR IMPROVEMENT IN THE FORMS OF PROCEEDING 38 (2d ed. 1846). Calvert described it as a "Pamphlet," and explained that "[t]he object of it is to suggest a system, by which the disputes of shareholders of joint stock companies *inter se* may be adjusted in a Court of Equity with the least possible inconvenience." *Id.* at 2.

37 F. CALVERT, A TREATISE UPON THE LAW RESPECTING PARTIES TO SUITS IN EQUITY 68 (2d ed. 1847). Professor Chafee termed it a work of "learned obscurity." CHAFEE, *supra*, at 200.

appealing from said Decree." *Giffard* v. *Hort*, 1 Sch. & Lef. 386, 411 (Ir. Ch. 1804, H.L. 1805).[38]

Justice Story summarized similar equity practice in the United States: "This Court will not suffer its jurisdiction to be ousted by the mere joinder or non-joinder of formal parties; but will rather proceed without them, and decide upon the merits of the case between the parties, who have the real interests before it, whenever it can be done without prejudice to the rights of others." *Wormley* v. *Wormley*, 8 Wheat. 421, 451 (1823). Respecting the latter point, he had suggested, as is incompletely quoted at Pet. Br. 20, that absent individuals could seek "other equitable relief, if their rights are jeoparded"—not that they could appeal. *West* v. *Randall*, 29 Fed. Cas. 718, 723 (C.C.D.R.I. 1820) (No. 17,424).[39] This Court later held that due process guarantees would not permit absent individuals to be bound by adjudications of their personal rights without adequate notice, representation and opportunity to be heard. *Hansberry* v. *Lee*, *supra*, 311 U.S. at 41-42 (1940) (citing *West*); see also *Phillips Pet. Co.* v. *Shutts*, *supra*, 472 U.S. at 811-12.[40]

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[38] CALVERT, *supra* n.37, at 66. See also *Osborne* v. *Usher*, 6 Bro. P.C. 20, 2 Eng. Rep. 905 (H.L. 1721) (remainderman of entailed estate had standing to appeal). Commenting on that case and others, Lord Eldon later observed that "it is very dangerous to trust to loose doctrines in old cases." *Lloyd* v. *Johnes*, 9 Ves. Jun. 37, 55, 32 Eng. Rep. 514, 521 (Ch. 1804).

[39] Justice Story in his discussion in *West* had noted the English terminology of "*quasi* parties." 29 Fed. Cas. at 723. He repeated it in his treatise. See J. STORY, COMMENTARIES ON EQUITY PLEADING 96 (2d ed. 1840) ("they may come in, or show it to be erroneous, or entitle themselves to a rehearing").

[40] CalPERS and FSBA have not attempted to question that Rule 23.1 satisfies due process. A student note cited by CalPERS and FSBA relied on the statements of Calvert and Story to conclude that there had been "a long history of taking a liberal view of appeals by unnamed 'class members'" in circumstances where their personal claims had been adjudicated. Comment, *The Appealability of Class Action Settlements by Unnamed Parties*, 60 U. CHI. L. REV. 933, 941 (1993); *cf. Gottlieb* v. *Wiles*, *supra*, 11 F.3d at 1012 n.7 ("we disagree with this student's analysis").

III. NON-PARTY APPEALS WOULD NOT BE CONFINED TO DERIVATIVE ACTIONS.

A. Non-Party Shareholder Appeals Would Mean Non-Party Appeals in Class Actions.

The procedural virus CalPERS and FSBA propose to release would infect other litigation. Rule 23(e), dealing with settlements of class actions, is an almost verbatim copy of the corresponding sentence of Rule 23.1. If the Federal Rules entitle non-parties to appeal in shareholder derivative actions, then will not the same words allow nonparties in class actions to appeal as well? Class actions are, indeed, an *a fortiori* case.[41] As the Court of Appeals pointed out, unlike the non-party shareholder in a derivative action, the class member has at stake a personal legal claim.[42] P.C.A. 4a-5a. In fact, two *amici* who often pursue class actions observe that "the question of appealability in the Rule 23 context is closely related to appealability in a Rule 23.1 derivative action, and thus it is likely that the decision of this Court will answer the Rule

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[41] "[T]he effect of a Rule 23.1 judgment on the absent shareholders is less significant than that of a Rule 23 judgment. Unlike a class action, the shareholder-plaintiff is not seeking to enforce an individual right belonging to each of the shareholders; he is suing on behalf of the corporation. . . . Moreover, the judgment in a derivative suit will not preclude any right of action that an absent shareholder might have in this individual capacity against the corporation or the real defendants in the derivative suit." 7C C. WRIGHT, *et al.*, *supra*, at 198 (footnote omitted).

[42] The additional provisions for notice, appearance and opportunity to opt out that Rule 23 provides to members of a class, but are absent in Rule 23.1, reflect heightened due process concerns that do not apply in shareholder derivative actions. See Advisory Committee Note, 39 F.R.D. 69, 106-07 (1966), citing *Hansberry* v. *Lee*, *supra*. CalPERS and FSBA oddly argue that "the case for the appellate rights of objectors is stronger in the derivative suit context because absent shareholders (unlike absent class members) have no ability to opt out of the suit." Pet. Br. 18 n.16. But the reason Rule 23.1 does not provide for opting out, of course, is that their own legal rights are not being adjudicated. Assuming fair and adequate representation, "one shareholder is interchangeable with any other shareholder in such suits." Z. CHAFEE, *supra*, at 222.

23 issue as well." Pub. Cit. Br. 4. CalPERS and FSBA themselves concede that "[t]he same basic rationale permits appeals by objecting class members in a Rule 23 class action." Pet. Br. 18 n.16.

There were 1,223 new class actions filed in the federal courts in 1996, and 1,709 in 1997.[43] Rule 23(e) and Rule 23.1 have the same operative language, which by ordinary rules of construction must mean for each the same thing. Of course, a line could be drawn arbitrarily limiting non-party appeals to derivative actions—but only by amending the Federal Rules.

B. Non-Party Appeals Would Unsettle Litigation of Many Other Kinds.

Even beyond class actions, if non-party shareholder appeals were authorized, then disgruntled non-parties would be able to claim a right to appeal without intervention in many other kinds of litigations well—a great variety of cases affecting groups of people. *Cf., e.g., New York* v. *Rebok Int'l, Ltd.*, 96 F.3d 44, 48 (2d Cir. 1996) (holding that under *Marino* non-parties could not appeal settlement of *parens patriae* litigation).

Flinching at the consequences of letting the barrier down, the government urgently cautions that "in only limited circumstances may a person who is not formally a named party to a case be regarded as a quasi party." G. Br. 15. It warns against "the potential for uncertain application of this Court's quasi party cases in other contexts," and urges that "recognition of quasi party status in situations not covered in the federal rules of procedure should be sparing indeed." *Id.* at 16. The government also asks that even in derivative suits, non-party appeals should be confined to objections to settlements—which it chooses, without any basis at all since a settlement resolves the complaint, to characterize as "ancillary." *Id.* at 16-17.

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[43] ADMINISTRATIVE OFFICE OF THE UNITED STATES COURTS, STATISTICAL TABLES FOR THE FEDERAL JUDICIARY, DECEMBER 31, 1997, Table X-5 (1998).

The government is particularly vehement that it must be exempted from the rule it seeks for others. There are to be no non-party appeals for the cases it wants to settle. "[A] citizen who objects to entry of a government-sponsored settlement decree," says the government, should not be allowed to conduct a non-party appeal even when a statute has guaranteed a right to object. G. Br. 18 & n.13.[44] This, says the government, is because it enjoys "special status as champion of the public interest" and "represent[s] the public interest at large (as opposed to a corporation's financial interest)." G. Br. 18 n.13.

Such line-drawing could perhaps be envisioned if the Federal Rules were amended. But there is not a word in the Federal Rules on which to base such sorting out of the non-party appeals the government wants from those it does not want. What the government is offering amounts to a legislative proposal. The government is really asking this Court to use adjudication to draft a new rule.[45]

IV. CALPERS' AND FSBA'S POLICY ARGUMENTS ARE INCOMPLETE AND MISDIRECTED.

A. CalPERS' and FSBA's Policy Arguments Rest on Flawed Assumptions and Ignore Competing Policies.

CalPERS and FSBA have been able to assemble a pile of *amicus* briefs, including not only one from their own Council of Institutional Investors, see J.A. 298, 318, but two others that the Council in turn has funded. See Barclays Br. 1-2 n.1; Hamermesh Br. 1 n.1. What is striking about such submissions is that in large measure they are scarcely legal analyses at all, but rather policy arguments that resemble testimony at a Congressional hearing.

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[44] Citing statutory rights to object to settlements provided in Antitrust Procedures and Penalties Act, 15 U.S.C. § 16(f)(3), CERCLA, 42 U.S.C. § 9622(d)(2), and Solid Waste Disposal Act, 42 U.S.C. § 6973(d), as well as 28 C.F.R. § 50.7 (settlements of pollution claims).

[45] *Cf.* 28 U.S.C. § 473(c) (exempting government litigation from some settlement procedures of Civil Justice Reform Act).

CalPERS and FSBA contend that if they are denied their wish to appeal as non-parties, "[t]hat unfortunate consequence would not be offset by *any* countervailing benefit." Pet. Br. 12 (emphasis in original); see also *id.* at 15-16 ("without furthering any countervailing policies"); see also CII Br. at 16 ("without providing any offsetting benefit"), 21 ("no corresponding benefit"), 26 ("without any corresponding benefit"). In reality, however, there are significant practical and policy considerations on the other side.

1. *CalPERS' and FSBA's Arguments Assume Inadequate Representation and Faulty Judicial Performance.*

CalPERS and FSBA say they fear "more approvals of inadequate and collusive derivative suit settlements." Pet. Br. 12. They and their supporting *amici* assert that unless objecting shareholders are allowed to appeal without intervention under the Federal Rules, district court settlements will not receive adequate appellate supervision. See Pet. Br. 32-34; CII Br. 16-28; Pub. Cit. Br. 22-23; G. Br. 21-24. They never really explain, however, why the appeals available to shareholders who comply with the Federal Rules are not enough. To say that "[o]nly objecting shareholders can give a federal court the benefit of an adversarial presentation," Pet. Br. 32, is no answer. At issue is not whether objectors may express their views to the district court without intervening (they can), nor even whether intervening objectors may appeal (they can), but rather whether an objector may decline to intervene, yet then appeal nevertheless. *Cf. In re Asbestos Litig.*, 90 F.3d 963, 990 (5th Cir. 1996) (dismissing appeals of objectors in class action who had not intervened, but deciding appeals of those who had done so), *vacated on other grounds*, 117 S. Ct. 2503 (1997), *on remand*, 134 F.3d 668 (5th Cir.), *cert. granted sub nom. Ortiz* v. *Fibreboard Corp.*, 118 S. Ct. 2339 (1998).

There is no empirical evidence that district courts regularly shirk their responsibilities in evaluating the fairness of settlements under Rule 23.1. District-court rejections of

derivative-action settlements regularly occur.[46] A computer search for the period 1971-1996 identified 25 reported appeals from federal district court approvals of settlements of derivative litigation, of which 20 resulted in affirmance.[47] Of the other five, only one rejected a settlement on the merits.[48] Similarly, a study of class

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[46] *E.g.*, among reported disapprovals, *In re Oracle Securities Litig.*, 829 F. Supp. 1176, 1190 (N.D. Cal. 1993) (disapproving settlement); *Krasner* v. *Dreyfus Corp.*, 500 F. Supp. 36, 45 (S.D.N.Y. 1980) (conditionally disapproving settlement); *Goldsholl* v. *Shapiro*, 417 F. Supp. 1291, 1300 (S.D.N.Y. 1976) (disapproving settlement).

[47] *City Partnership Co.* v. *Atlantic Acquisition Ltd. Partnership*, 100 F.3d 1041 (1st Cir. 1996); *In re Pacific Enterprises Securities Litig.*, 47 F.3d 373 (9th Cir. 1995); *Ackerman* v. *Kassar*, 5 F.3d 534 (9th Cir. 1993) (table); *Bell Atlantic Corp.* v. *Bolger*, 2 F.3d 1304 (3rd Cir. 1993); *Granada Investments, Inc.* v. *DWG Corp.*, 962 F.2d 1203 (6th Cir. 1992); *Zarowitz* v. *Bankamerica Corp.*, 866 F.2d 1164 (9th Cir. 1989); *Zimmerman* v. *Bell*, 800 F.2d 386 (4th Cir. 1986); *In re Warner Communications Securities Litig.*, 798 F.2d 35 (2nd Cir. 1986); *Wiener* v. *Roth*, 791 F.2d 661 (8th Cir. 1986); *Jones* v. *Nuclear Pharmacy, Inc.*, 741 F.2d 322 (10th Cir. 1984); *In re General Tire & Rubber Co. Securities Litig.*, 726 F.2d 1075 (6th Cir. 1984), *cert. denied*, 469 U.S. 858 (1984); *Blatt* v. *Dean Witter Reynolds Intercapital, Inc.*, 732 F.2d 304 (2d Cir. 1984); *TBK Partners, Ltd.* v. *Western Union Corp.*, 675 F.2d 456 (2d Cir. 1982); *Maher* v. *Zapata Corp.*, 714 F.2d 436 (5th Cir. 1983); *Shlensky* v. *Dorsey*, 574 F.2d 131 (3d Cir. 1978) (affirming settlement, remanding on attorneys' fees); *Miller* v. *Republic Nat'l Life Ins. Co.*, 559 F.2d 426 (5th Cir. 1977); *Pearson* v. *Ecological Science Corp.*, 522 F.2d 171 (5th Cir. 1975), *cert. denied*, 425 U.S. 912 (1976); *Greenspun* v. *Bogan*, 492 F.2d 375 (1st Cir. 1974); *Wesson* v. *Mississippi River Corp.*, 486 F.2d 1398 (2d Cir.) (table), *cert. denied*, 414 U.S. 1112 (1973); *United Founders Life Ins. Co.* v. *Consumers Nat'l Life Ins. Co.*, 447 F.2d 647 (7th Cir. 1971). There were at least six, not four, such appeals since 1990, listed *supra* and in n.48, *infra*. *Cf.* Pet. Br. 37-38 n.37.

[48] See *In re Pittsburgh & L.E.R.R. Securities and Antitrust Litig.*, 543 F.2d 1058 (3d Cir. 1976) (holding district court abused its discretion); see also *Rosenbaum* v. *MacAllister*, 64 F.3d 1439 (10th Cir. 1995) (remanding for evidentiary hearing on attorneys' fees); *Clark* v. *Lomas & Nettleton Financial Corp.*, 625 F.2d 49 (5th Cir. 1980) (vacating because directors not competent to settle), *cert. denied*, 450 U.S. 1029 (1981); *Saylor* v. *Bastedo*, 623

actions in four federal judicial districts confirmed that "Few of the appeals resulted in altering the prior decision of the trial judge." T. WILLGING, *et al.*, EMPIRICAL STUDY OF CLASS ACTIONS IN FOUR FEDERAL DISTRICT COURTS 82 (Fed. Judicial Ctr. 1996). *Cf. Evans* v. *Jeff D.*, 475 U.S. 717, 742 (1986) ("we shall rely primarily on the sound discretion of the district courts").

2. Non-Party Appeals Are Not Essential To Protect Objecting Shareholders.

Not to permit non-party shareholder appeals scarcely prevents judicial review, including appellate review, of derivative-action settlements. It has often been noted that such non-parties have a number of options.[49] In the first place, any shareholder may bring a derivative action. CalPERS and FSBA chose not to exercise that option, preferring instead to be free riders and have others perform that task.[50] They also, of course, could have sought to intervene, before or after judgment; they elected not to do that, either. They were prevented from appealing, not by any difficult obstacles created by the Federal Rules, but rather by their own choice. An *amicus* brief asks this Court in applying the Federal Rules to take pity on the plight of the large investor, able to function on Wall Street but described as too bureaucratic and slow to respond to

F.2d 230 (2d Cir. 1980) (reversing for procedural error); *Girsh* v. *Jepson*, 521 F.2d 153 (3d Cir. 1975) (reversing for insufficient notice and discovery).

[49] See *Shults* v. *Champion Int'l Corp.*, *supra*, 35 F.3d at 1058-59; *Croyden Assocs.* v. *Alleco, Inc.*, *supra*, 969 F.2d at 678; *Walker* v. *City of Mesquite*, *supra*, 858 F.2d at 1073-75; *Guthrie* v. *Evans*, *supra*, 815 F.2d at 628.

[50] At the same time, their association, CII, laments the unwillingness of institutional investors to become named plaintiffs in shareholder securities litigation. CII Br. at 25. *Cf.* Weiss & Beckerman, *Let the Money Do the Monitoring: How Institutional Investors Can Reduce Agency Costs in Securities Class Actions*, 104 YALE L.J. 2053, 2095 (1995) (noting that rather than becoming lead plaintiffs or intervening, institutional investors "have sat on the sidelines").

the supposed lightning pace of shareholder litigation.[51] *But cf. Eisen* v. *Carlisle & Jacquelin*, *supra*, 417 U.S. at 176 (rejecting argument that Rule 23's requirements "can be tailored to fit the pocketbooks of particular plaintiffs").

Moreover, in a case of real collusion or fraud at the expense of the corporation, or gross malfeasance by its board of directors in settling a derivative suit—something CalPERS and FSBA did not even attempt to show here, see J.A. 338—a non-party shareholder would not be precluded from bringing a separate derivative action to challenge the settlement. *Cf. Matsushita Elec. Indus. Co.* v. *Epstein*, 516 U.S. 367, 396 (1966) (Ginsburg, J., concurring and dissenting); *Hansberry* v. *Lee*, *supra*; *Wolf* v. *Barkes*, 348 F.2d 994 (2d Cir.), *cert. denied*, 382 U.S. 941 (1965). In class actions "it is recognized that under circumstances of inadequate representation, relief may be pursued in a collateral proceeding." *Guthrie* v. *Evans*, *supra*, 815 F.2d at 628; *Shults* v. *Champion Int'l Corp.*, *supra*, 35 F.3d at 1058.

3. Non-Party Appeals Would Make Settlements More Difficult, Costly and Uncertain.

Besides disrupting the appellate process, the rule that CalPERS and FSBA seek would be frankly designed to make settlement of shareholder derivative actions more difficult. See Pet. Br. 32-33; G. Br. 22-24. Yet traditionally and with good reason, the general policy of the law has been to favor, not discourage, settlements. See, *e.g.*, *McDermott, Inc.* v. *AmClyde*, 511 U.S. 202, 215 (1994) ("public policy wisely encourages settlements"); *Donovan* v. *Robbins*, 752 F.2d 1170, 1177 (7th Cir. 1985) ("settlements are favored and ordinarily should be approved"); *cf. Carson* v. *American Brands, Inc.*, 450 U.S. 79, 89-90

[51] According to the Barclays Global Investors Brief, large institutional investors have a "lengthy decision-making process" and only "limited resources for coping with the larger responsibilities associated with intervention"—although the signatories to that brief say they control "about $9.5 trillion in assets." Barclays Br. at 11, 5, 2.

(1981) (order preventing settlement immediately appealable). Encouragement of settlements is a policy also endorsed by Congress, see 28 U.S.C. §§ 473(a)(3)(A), 473(b)(5); Fed. R. Evid. 408 and Advisory Committee Note, 56 F.R.D. 187, 227 (1972) ("public policy favoring the compromise and settlement of disputes"). It is also written into several of the Federal Rules. See Fed. R. Civ. P. 16(a)(5) ("facilitating the settlement of the case" an objective of pretrial conference); Fed. R. Civ. P. 68 (enforceable offer of judgment); see *Marek* v. *Chesny*, 473 U.S. 1, 5 (1985). In addition, many federal Circuits have adopted rules that require participation in pre-appeal settlement conferences.[52]

CalPERS and FSBA can scarcely argue that a non-party appeal is necessary to benefit ADM and its shareholders. ADM's new board of directors, which is responsible for managing the company, voted to settle these sixteen lawsuits, to end the time and money drain of litigation. J.A. 112. And ADM's shareholders themselves just two years ago considered the very same proposals that CalPERS and FSBA seek to have a court impose—and voted them down. J.A. 308, 318-19. None of ADM's 365 other institutional shareholders objected to the proposed settlement. Only five objections from its other approximately 243,000 shareholders were submitted. *See* n.6, *supra*. "For aught that appears, the course pursued by the directors has the approval of all the stockholders except the plaintiffs." *United Copper Securities Co.* v. *Amalgamated Copper Co.*, 244 U.S. 261, 264 (1917) (Brandeis, J.); see also *Hawes* v. *Oakland*, *supra*, 104 U.S. at 462 ("[t]he great body of the stockholders . . . may take this view of it, and be content to abide by the action of their directors"). Finally, one may note that CalPERS and FSBA, who say that they "awarded ADM a grade of 'F'" under its former board of directors, Pet. Br. 4, have not sold

[52] See First Circuit Rule 47.5; Second Circuit Rules, App. C; Sixth Circuit Rule 18; Ninth Circuit Rule 33-1; Tenth Circuit Rule 33.1; Eleventh Circuit Rule 33-1; D.C. Circuit Rules, App. III; Federal Circuit Rule 33.

their stock in ADM. Apparently CalPERS' and FSBA's money managers are less dismayed than their lawyers.

4. Non-Party Appeals Would Proliferate and Confuse Appellate Litigation.

CalPERS and FSBA assert that not to allow non-parties to appeal "would dramatically decrease [the] number" of appeals challenging settlements, Pet. Br. 33—even though most Circuits do not allow non-party appeals now, and intervention under Rule 24 remains available. They regard low numbers of appeals of derivative action settlements as a cause for concern, and assume that adding to the appellate dockets more litigation from shareholders unwilling to intervene would be a good thing. Pet. Br. 37-38. But the soundness of their view is not self-evident. Might a paucity of appeals not reflect that most such settlements are widely welcomed? And that district courts, who have been assigned broad discretion whether to approve, usually are adequately doing their jobs?[53] Is the blocking or challenging of more settlements for the duration of an appellate process a public benefit? That the ruling sought here would indeed mean more appeals, they say, "[t]here is . . . no question." *Id.* at 34.

B. Policy Arguments Should Be Directed to Congress or the Rules Advisory Committees.

The appropriate policies for conducting shareholder derivative actions and class actions are a topic of neither consensus nor neglect. "[S]hareholder derivative suits have been controversial since their inception." Swanson, *Corporate Governance: Sliding Seamlessly into the Twenty-First Century*, 21 J. CORP. LAW 417, 437 (1996). *Cf. Cohen* v. *Beneficial Indus. Loan Corp.*, 337 U.S. 541, 551 (1949): "In dealing with such difficult and controversial subjects, only experience will verify or disclose weaknesses

[53] See *City Partnership Co.* v. *Atlantic Acquisition Ltd. Partnership*, 100 F.3d 1041, 1043-44 (1st Cir. 1996); *Granada Investments, Inc.* v. *DWG Corp.*, 962 F.2d 1203, 1205 (6th Cir. 1992); *Maher* v. *Zapata Corp.*, 714 F.2d 436, 455 (5th Cir. 1983).

and defects of any policy and teach lessons which may be applied by amendment."

A case this Court decided the same year as *Marino* illustrates the most fundamental flaw in CalPERS' and FSBA's plethora of policy arguments. In *Torres* v. *Oakland Scavenger Co.*, 487 U.S. 312 (1988), parties not named in a notice of appeal were dismissed because of Appellate Rule 3(c)'s requirement that the notice of appeal "must specify the party or parties taking the appeal." Declining to consider policy arguments, this Court looked to the text of Rule 3(c), explaining that "we are convinced that the harshness of our construction is 'imposed by the legislature and not by the judicial process.'" 487 U.S. at 318, quoting *Schiavone* v. *Fortune*, 477 U.S. 21, 31 (1986).[54] Soon thereafter Rule 3(c) was amended to permit omission of the names of parties appealing as long as they were unambiguously described. 507 U.S. 1061, 1063 (1993); see Advisory Committee Note, 113 S. Ct. pref. 484, 487 (1992).[55]

Even to draft the procedure being asked for here would not be simple, and would require resolving many questions. CalPERS and FSBA apparently propose to limit non-party appeals to shareholders who appear in court and file objections. See Pet. Br. 15. Or perhaps to those who simply file them? Or to those who write a letter? Or who argue at a hearing? The government, on the other

[54] In *Torres* the dismissal resulted from a clerical error. In this case CalPERS and FSBA say that they had believed that the Seventh Circuit did not require intervention for appeals in derivative suits, Pet. Br. 9—even after the Seventh Circuit had already emphatically held that non-parties could not appeal even in class actions. See *In re Brand Name Drugs, supra*. Even if mistaken about the law, CalPERS and FSBA still could have requested leave to intervene in the Court of Appeals, but they did not do so.

[55] *Cf. also, e.g.*, 105 Stat. 1076 (1991), 42 U.S.C. § 2000e-2(n), enacted after *Martin* v. *Wilks*, 490 U.S. 755 (1989), to alter procedure for notice of and objections to Title VII consent decrees, see G. Br. 26 n.20; 105 Stat. 2387 (1991), 15 U.S.C. § 78aa-1 (overruling retroactive application of *Lampf, Pleva, Lipkind, Prupis & Petigrow* v. *Gilbertson*, 501 U.S. 350 (1991)).

hand, contemplates a right of appeal for any shareholder "who submits an objection," G. Br. 1—always excepting however, challenges to its own settlements. See pp. 40-41, *supra*. Such lines cannot be extracted from the text of any of the present Federal Rules. But they could be debated and devised if Congress acted or the Rules were amended. In *Martin* v. *Wilks*, 490 U.S. 755, 767 (1989), this Court in declining to adopt a proposed interpretation of other Federal Rules regarding parties explained that "Even if we were wholly persuaded by these arguments as a matter of policy, acceptance of them would require a rewriting rather than an interpretation of the relevant rules."

How shareholder derivatives suits and class actions should be conducted and adjudicated remains among the most contentious issues of public policy today. CalPERS and FSBA note that "Congress . . . changed many of the procedural rules associated with securities class actions." Pet. Br. 37 n.35. The past two Congresses have acted twice to regulate the conduct of representative securities suits in the federal courts. Private Securities Litigation Reform Act of 1995, 109 Stat. 737, 15 U.S.C. §§ 78u-4(a)(3)(B)(iii)(I), 78u-4(a)(7) (preference that large investors be lead class-action plaintiffs; special notice provisions to shareholders) (enacted over veto); Securities Litigation Uniform Standards Act of 1998, 112 Stat. 3227. Bills on these subjects continue to be introduced and hearings held;[56] but as in some related controversial areas, "Congress, however, has not adopted such a solution." *Amchem Prods., Inc.* v. *Windsor, supra*, 117 S. Ct. at 2252. "[T]he proper venue for resolving that issue remains the floor of Congress." *Lexecon, Inc.* v. *Milberg Weiss Bershad Hynes & Lerach*, 118 S. Ct. 956, 964 (1998).

[56] *E.g.*, in the 105th Congress, H.R. 660, H.R. 1689, H.R. 1252, H.R. 1283, H.R. 3789, S. 2083. See, *e.g.*, *Class Action Lawsuits: Examining Victim Compensation and Attorneys' Fees*, Hearing before Subcomm. on Admin. Oversight and the Courts, Senate Comm. on Judiciary, 105th Cong., 1st Sess. 37 (1997) (report of Judge Niemeyer on Rules changes adopted and considered, stating that "we wish to work with Congress on these issues").

In addition, the Judicial Code provides for a rulemaking process, assigned to this Court, 28 U.S.C. § 2072, and conducted by the Advisory Committees established by the Judicial Conference, subject to this Court's and Congressional oversight. *Cf.* Order, 507 U.S. 1091 (1993) (Statement of Justice White). The Federal Rules are constantly reviewed by the Advisory Committees and regularly amended in light of experience. *E.g.*, Order, 118 S. Ct. pref. 399 (1998) (amending Fed. R. Civ. P. 23 to allow interlocutory appeals of class certification); id. at 405 (revising Fed. R. App. P. 3).[52]

In the last footnote of its brief, the government acknowledges the proper way to resolve contentious policy issues of procedure for shareholder litigation: "In the alternative, the Federal Rules of Civil and Appellate Procedure could be amended to address the problem." G. Br. 29 n.23. Exactly so.

CONCLUSION

For the reasons stated, certiorari should be dismissed or the judgment of the Court of Appeals affirmed.

Respectfully submitted,

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[57] Between 1962 and 1993, Federal Rules were adopted or amended 64 times. See Order, 507 U.S. 1091, 1092 (Statement of White, J). See also Proposed Amendments to Federal Rules of Civil Procedure, 119 S. Ct. CtR 163, 186 (1998) (Advisory Committee request for comments on proposed amendments to Federal Rules); *cf.* Schwarzer, *Settlement of Mass Tort Class Actions: Order Out of Chaos*, 80 CORN. L. REV. 837, 843 (1995) ("Amendment of Rule 23(e) is . . . worthy of consideration").

ADDENDUM

ADDENDUM

TITLE 28 UNITED STATES CODE

Section 1254 provides:

Courts of appeals; certiorari; certified questions

Cases in the courts of appeals may be reviewed by the Supreme Court by the following methods:

(1) By writ of certiorari granted upon the petition of any party to any civil or criminal case, before or after rendition of judgment or decree;

(2) By certification at any time by a court of appeals of any question of law in any civil or criminal case as to which instructions are desired, and upon such certification the Supreme Court may give binding instructions or require the entire record to be sent up for decision of the entire matter in controversy.

Former § 1254, prior to amendment in 1988, 102 Stat. 662, provided:

Courts of appeals; certiorari; appeal; certified questions.

Cases in the courts of appeals may be reviewed by the Supreme Court by the following methods:

(1) By writ of certiorari granted upon the petition of any party to any civil or criminal case, before or after rendition of judgment or decree;

(2) By appeal by a party relying on a State statute held by a court of appeals to be invalid as repugnant to the Constitution, treaties or laws of the United States, but such appeal shall

preclude review by writ of certiorari at the instance of such appellant, and the review on appeal shall be restricted to the Federal questions presented;

(3) By certification at any time by a court of appeals of any question of law in any civil or criminal case as to which instructions are desired, and upon such certification the Supreme Court may give binding instructions or require the entire record to be sent up for decision of the entire matter in controversy.

FEDERAL RULES OF CIVIL PROCEDURE

Rule 23 provides:

Class Actions

(a) **Prerequisites to a Class Action.** One or more members of a class may sue or be sued as representative parties on behalf of all only if (1) the class is so numerous that joinder of all members is impracticable, (2) there are questions of law or fact common to the class, (3) the claims or defenses of the representative parties are typical of the claims or defenses of the class, and (4) the representative parties will fairly and adequately protect the interests of the class.

(b) **Class Actions Maintainable.** An action may be maintained as a class action if the prerequisites of subdivision (a) are satisfied, and in addition:

(1) the prosecution of separate actions by or against individual members of the class would create a risk of

(A) inconsistent or varying adjudications with respect to individual members of the class which would establish incompatible standards of conduct for the party opposing the class, or

(B) adjudications with respect to individual members of the class which would as a practical matter be dispositive of the interests of the other members not parties to the adjudications or substantially impair or impede their ability to protect their interests; or

(2) the party opposing the class has acted or refused to act on grounds generally applicable to the class, thereby making appropriate

final injunctive relief or corresponding declaratory relief with respect to the class as a whole; or

(3) the court finds that the questions of law or fact common to the members of the class predominate over any questions affecting only individual members, and that a class action is superior to other available methods for the fair and efficient adjudication of the controversy. The matters pertinent to the findings include: (A) the interest of members of the class in individually controlling the prosecution or defense of separate actions; (B) the extent and nature of any litigation concerning the controversy already commenced by or against members of the class; (C) the desirability or undesirability of concentrating the litigation of the claims in the particular forum; (D) the difficulties likely to be encountered in the management of a class action.

(c) **Determination by Order Whether Class Action to be Maintained; Notice; Judgment; Actions Conducted Partially as Class Actions.**

(1) As soon as practicable after the commencement of an action brought as a class action, the court shall determine by order whether it is to be so maintained. An order under this subdivision may be conditional, and may be altered or amended before the decision on the merits.

(2) In any class action maintained under subdivision (b)(3), the court shall direct to the members of the class the best notice practicable under the circumstances, including individual notice to all members who can be identified through reasonable effort. The notice shall advise each member that (A) the court will exclude the member from the class if the member so requests by a specified date; (B) the judgment, whether favorable or not, will include all members who do not request exclusion; and (C) any member who does not request exclusion may, if the member desires, enter an appearance through counsel.

(3) The judgment in an action maintained as a class action under subdivision (b)(1) or (b)(2), whether or not favorable to the class, shall include and describe those whom the court finds to be members of the class. The judgment in an action maintained as a class action under subdivision (b)(3), whether or not favorable to the class, shall include and specify or describe those to whom the notice provided in subdivision (c)(2) was directed, and who have not requested exclusion, and whom the court finds to be members of the class.

(4) When appropriate (A) an action may be brought or maintained as a class action with respect to particular issues, or (B) a class may be divided into subclasses and each subclass treated as a class, and the provisions of this rule shall then be construed and applied accordingly.

(d) **Orders in Conduct of Actions.** In the conduct of actions to which this rule applies, the court may make appropriate orders: (1) determining the course of proceedings or prescribing measures to prevent undue repetition or complication in the presentation of evidence or argument; (2) requiring, for the protection of the members of the class or otherwise for the fair conduct of the action, that notice be given in such manner as the court may direct to some or all of the members of any step in the action, or of the proposed extent of the judgment, or of the

opportunity of members to signify whether they consider the representation fair and adequate, to intervene and present claims or defenses, or otherwise to come into the action; (3) imposing conditions on the representative parties or on intervenors; (4) requiring that the pleadings be amended to eliminate therefrom allegations as to representation of absent persons, and that the action proceed accordingly; (5) dealing with similar procedural matters. The orders may be combined with an order under Rule 16, and may be altered or amended as may be desirable from time to time.

(e) **Dismissal or Compromise.** A class action shall not be dismissed or compromised without the approval of the court, and notice of the proposed dismissal or compromise shall be given to all members of the class in such manner as the court directs.

(f) **Appeals.** A court of appeals may in its discretion permit an appeal from an order of a district court granting or denying class action certification under this rule if application is made to it within ten days after entry of the order. An appeal does not stay proceedings in the district court unless the district judge or the court of appeals so orders.

Rule 23.1 provides:

Derivative Actions by Shareholders

In a derivative action brought by one or more shareholders or members to enforce a right of a corporation or of an unincorporated association, the corporation or association having failed to enforce a right which may properly be asserted by it, the complaint shall be verified and shall allege (1) that the plaintiff was a shareholder or member at the time of the transaction of which the plaintiff complains or that the plaintiff's share or membership thereafter devolved on the plaintiff by operation of law, and (2)

that the action is not a collusive one to confer jurisdiction on a court of the United States which it would not otherwise have. The complaint shall also allege with particularity the efforts, if any, made by the plaintiff to obtain the action the plaintiff desires from the directors or comparable authority and, if necessary, from the shareholders or members, and the reasons for the plaintiff's failure to obtain the action or for not making the effort. The derivative action may not be maintained if it appears that the plaintiff does not fairly and adequately represent the interests of the shareholders or members similarly situated in enforcing the right of the corporation or association. The action shall not be dismissed or compromised without the approval of the court, and notice of the proposed dismisal or compromise shall be given to shareholders or members in such manner as the court directs.

Rule 24 provides:

Intervention

(a) **Intervention of Right.** Upon timely application anyone shall be permitted to intervene in an action: (1) when a statute of the United States confers an unconditional right to intervene; or (2) when the applicant claims an interest relating to the property or transaction which is the subject of the action and the applicant is so situated that the disposition of the action may as a practical matter impair or impede the applicant's ability to protect that interest, unless the applicant's interest is adequately represented by existing parties.

(b) **Permissive Intervention.** Upon timely application anyone may be permitted to intervene in an action: (1) when a statute of the United States confers a conditional right to intervene; or (2) when an applicant's claim or defense and the main action have a question of law or fact in common. When a

party to an action relies for ground of claim or defense upon any statute or executive order administered by a federal or state governmental officer or agency or upon any regulation, order, requirement, or agreement issued or made pursuant to the statute or executive order, the officer or agency upon timely application may be permitted to intervene in the action. In exercising its discretion the court shall consider whether the intervention will unduly delay or prejudice the adjudication of the rights of the original parties.

(c) **Procedure.** A person desiring to intervene shall serve a motion to intervene upon the parties as provided in Rule 5. The motion shall state the grounds therefor and shall be accompanied by a pleading setting forth the claim or defense for which intervention is sought. The same procedure shall be followed when a statute of the United States gives a right to intervene. When the constitutionality of an act of Congress affecting the public interest is drawn in question in any action in which the United States or an officer, agency, or employee thereof is not a party, the court shall notify the Attorney General of the United States as provided in Title 28, U.S.C. § 2403. When the constitutionality of any statute of a State affecting the public interest is drawn in question in any action in which that State or any agency, officer, or employee thereof is not a party, the court shall notify the attorney general of the State as provided in Title 28, U.S.C. § 2403. A party challenging the constitutionality of legislation should call the attention of the court to its consequential duty, but failure to do so is not a waiver of any constitutional right otherwise timely asserted.

Former Rule 73, 309 U.S. 749 (1938), provided in part:

Appeal to a Circuit Court of Appeals.

(a) How Taken. When an appeal is permitted by law from a district court to a circuit court of appeals and within the time prescribed, a party may appeal from a judgment by filing with the district court a notice of appeal. Failure of the appellant to take any of the further steps to secure the review of the judgment appealed from does not affect the validity of the appeal, but is ground only for such remedies as are specified in this rule or, when no remedy is specified, for such action as the appellate court deems appropriate, which may include dismissal of the appeal.

(b) Notice of Appeal. The notice of appeal shall specify the parties taking the appeal; shall designate the judgment or part thereof appealed from; and shall name the court to which the appeal is taken. Notification of the filing of the notice of appeal shall be given by the clerk by mailing copies thereof to all the parties to the judgment other than the party or parties taking the appeal, but his failure so to do does not affect the validity of the appeal. The notification to a party shall be given by mailing a copy of the notice of appeal to his attorney of record or, if the party is not represented by an attorney, then to the party at his last known address, and such notification is sufficient notwithstanding the death of the party or of his attorney prior to the giving of the notification. The clerk shall note in the civil docket the names of the parties to whom he mails the copies, with date of mailing.

* * * *

FEDERAL RULES OF APPELLATE PROCEDURE

Rule 3 provides:

Appeal as of Right—How Taken

(a) **Filing the Notice of Appeal.**

(1) An appeal permitted by law as of right from a district court to a court of appeals may be taken only by filing a notice of appeal with the district clerk within the time allowed by Rule 4. At the time of filing, the appellant must furnish the clerk with enough copies of the notice to enable the clerk to comply with Rule 3(d).

(2) An appellant's failure to take any step other than the timely filing of a notice of appeal does not affect the validity of the appeal, but is ground only for the court of appeals to act as it considers appropriate, including dismissing the appeal.

(3) An appeal from a judgment by a magistrate judge in a civil case is taken in the same way as an appeal from any other district court judgment.

(4) An appeal by permission under 28 U.S.C. § 1292(b) or an appeal in a bankruptcy case may be taken only in the manner prescribed by Rules 5 and 6, respectively.

(b) **Joint or Consolidated Appeals.**

(1) When two or more parties are entitled to appeal from a district-court judgment or order, and their interests make joinder practicable, they may file a joint notice of appeal. They may then proceed on appeal as a single appellant.

(2) When the parties have filed separate timely notices of appeal, the appeals may be joined or consolidated by the court of appeals.

(c) **Contents of the Notice of Appeal.**

(1) The notice of appeal must:

(A) specify the party or parties taking the appeal by naming each one in the caption or body of the notice, but an attorney representing more than one party may describe those parties with such terms as "all plaintiffs," "the defendants," "the plaintiffs A, B, et al.," or "all defendants except X";

(B) designate the judgment, order, or part thereof being appealed; and

(C) name the court to which the appeal is taken.

(2) A pro se notice of appeal is considered filed on behalf of the signer and the signer's spouse and minor children (if they are parties), unless the notice clearly indicates otherwise.

(3) In a class action, whether or not the class has been certified, the notice of appeal is sufficient if it names one person qualified to bring the appeal as representative of the class.

(4) An appeal must not be dismissed for informality of form or title of the notice of appeal, or for failure to name a party whose intent to appeal is otherwise clear from the notice.

(5) Form 1 in the Appendix of Forms is a suggested form of a notice of appeal.

(d) **Serving the Notice of Appeal.**

(1) The district clerk must serve notice of the filing of a notice of appeal by mailing a copy to each party's counsel of record—excluding the appellant's—or, if a party is proceeding pro se, to the party's last known address. When a defendant in a criminal

case appeals, the clerk must also serve a copy of the notice of appeal on the defendant, either by personal service or by mail addressed to the defendant. The clerk must promptly send a copy of the notice of appeal and of the docket entries—and any later docket entries—to the clerk of the court of appeals named in the notice. The district clerk must note, on each copy, the date when the notice of appeal was filed.

(2) If an inmate confined in an institution files a notice of appeal in the manner provided by Rule 4(c), the district clerk must also note the date when the clerk docketed the notice.

(3) The district clerk's failure to serve notice does not affect the validity of the appeal. The clerk must note on the docket the names of the parties to whom the clerk mails copies, with the date of mailing. Service is sufficient despite the death of a party or the party's counsel.

(e) **Payment of Fees.** Upon filing a notice of appeal, the appellant must pay the district clerk all required fees. The district clerk receives the appellate docket fee on behalf of the court of appeals.

Rule 4 provides:

Appeal as of Right—When Taken

(a) **Appeal in a Civil Case.**

(1) *Time for Filing a Notice of Appeal.*

(A) In a civil case, except as provided in Rules 4(a)(1)(B), 4(a)(4), and 4(c), the notice of appeal required by Rule 3 must be filed with the district clerk within 30 days after the judgment or order appealed from is entered.

(B) When the United States or its officer or agency is a party, the notice of appeal may be filed by any party within 60 days after the judgment or order appealed from is entered.

(2) *Filing Before Entry of Judgment.* A notice of appeal filed after the court announces a decision or order—but before the entry of the judgment or order—is treated as filed on the date of and after the entry.

(3) *Multiple Appeals.* If one party timely files a notice of appeal, any other party may file a notice of appeal within 14 days after the date when the first notice was filed, or within the time otherwise prescribed by this Rule 4(a), whichever period ends later.

(4) *Effect of a Motion on a Notice of Appeal.*

(A) If a party timely files in the district court any of the following motions under the Federal Rules of Civil Procedure, the time to file an appeal runs for all parties from the entry of the order disposing of the last such remaining motion:

(i) for judgment under Rule 50(b);

(ii) to amend or make additional factual findings under Rule 52(b), whether or not granting the motion would alter the judgment;

(iii) for attorney's fees under Rule 54 if the district court extends the time to appeal under Rule 58;

(iv) to alter or amend the judgment under Rule 59;

(v) for a new trial under Rule 59; or

(vi) for relief under Rule 60 if the motion is filed no later than 10 days (computed using Federal Rule of Civil Procedure 6(a)) after the judgment is entered.

(B)(i) If a party files a notice of appeal after the court announces or enters a judgment—but before it disposes of any motion listed in Rule 4(a)(4)(A)—the notice becomes effective to appeal a judgment or order, in whole or in part, when the order disposing of the last such remaining motion is entered.

(ii) A party intending to challenge an order disposing of any motion listed in Rule 4(a)(4)(A), or a judgment altered or amended upon such a motion, must file a notice of appeal, or an amended notice of appeal—in compliance with Rule 3(c)—within the time prescribed by this Rule measured from the entry of the order disposing of the last such remaining motion.

(iii) No additional fee is required to file an amended notice.

(5) *Motion for Extension of Time.*

(A) The district court may extend the time to file a notice of appeal if:

(i) a party so moves no later than 30 days after the time prescribed by this Rule 4(a) expires; and

(ii) that party shows excusable neglect or good cause.

(B) A motion filed before the expiration of the time prescribed in Rule 4(a)(1) or (3) may be ex parte unless the court requires otherwise. If the motion is filed after the expiration of the prescribed time, notice must be given to the other parties in accordance with local rules.

(C) No extension under this Rule 4(a)(5) may exceed 30 days after the prescribed time or 10 days after the date when the order granting the motion is entered, whichever is later.

(6) *Reopening the Time to File an Appeal.* The district court may reopen the time to file an appeal for a period of 14 days after the date when its order to reopen is entered, but only if all the following conditions are satisfied:

(A) the motion is filed within 180 days after the judgment or order is entered or within 7 days after the moving party receives notice of the entry, whichever is earlier;

(B) the court finds that the moving party was entitled to notice of the entry of the judgment or order sought to be appealed but did not receive the notice from the district court or any party within 21 days after entry; and

(C) the court finds that no party would be prejudiced.

(7) *Entry Defined.* A judgment or order is entered for purposes of this Rule 4(a) when it is entered in compliance with Rules 58 and 79(a) of the Federal Rules of Civil Procedure.

* * * *

(d) **Mistaken Filing in the Court of Appeals.** If a notice of appeal in either a civil or a criminal case is mistakenly filed in the court of appeals, the clerk of that court must note on the notice the date when it was received and send it to the district clerk. The notice is then considered filed in the district court on the date so noted.

FEDERAL EQUITY RULES

Rule 94, 104 U.S. ix (1882), provided:

> Every bill brought by one or more stockholders in a corporation, against the corporation and other parties, founded on rights which may properly be asserted by the corporation, must be verified by oath, and must contain an allegation that the plaintiff was a shareholder at the time of the transaction of which he complains, or that his share had devolved on him since by operation of law; and that the suit is not a collusive one to confer on a court of the United States jurisdiction of a case of which it would not otherwise have cognizance. It must also set forth with particularity the efforts of the plaintiff to secure such action as he desires on the part of the managing directors or trustees, and, if necessary, of the shareholders, and the causes of his failure to obtain such action.

Rule 27, 226 U.S. 656 (1912), provided:

> Every bill brought by one or more stockholders in a corporation against the corporation and other parties, founded on rights which may properly be asserted by the corporation, must be verified by oath, and must contain an allegation that the plaintiff was a shareholder at the time of the transaction of which he complains, or that his share had devolved on him since by operation of law, and that the suit is not a collusive one to confer on a court of the United States jurisdiction of a case of which it would not otherwise have cognizance. It must also set forth with particularity the efforts of the plaintiff to secure such action as he desires on the part of the managing directors or trustees, and, if necessary, of the

shareholders, and the causes of his failure to obtain such action, or the reasons for not making such effort.

Rule 37, 226 U.S. 659 (1912), provided:

PARTIES GENERALLY—INTERVENTION.

Every action shall be prosecuted in the name of the real party in interest, but an executor, administrator, guardian, trustee of an express trust, a party with whom or in whose name a contract has been made for the benefit of another, or a party expressly authorized by statute, may sue in his own name without joining with him the party for whose benefit the action is brought. All persons having an interest in the subject of the action and in obtaining the relief demanded may join as plaintiffs, and any person may be made a defendant who has or claims an interest adverse to the plaintiff. Any person may at any time be made a party if his presence is necessary or proper to a complete determination of the cause. Persons having a united interest must be joined on the same side as plaintiffs or defendants, but when anyone refuses to join, he may for such reason be made a defendant.

Anyone claiming an interest in the litigation may at any time be permitted to assert his right by intervention, but the intervention shall be in subordination to, and in recognition of, the propriety of the main proceeding.

Rule 38, 226 U.S. 659 (1912), provided:

REPRESENTATIVES OF CLASS.

When the question is one of common or general interest to many persons constituting a class so numerous as to make it impracticable to bring them all before the court, one or more may sue or defend for the whole.

Rule 39, 226 U.S. 659 (1912), provided:

ABSENCE OF PERSONS WHO WOULD BE PROPER PARTIES.

In all cases where it shall appear to the court that persons, who might otherwise be deemed proper parties to the suit, cannot be made parties by reason of their being out of the jurisdiction of the court, or incapable otherwise of being made parties, or because their joinder would oust the jurisdiction of the court as to the parties before the court, the court may, in its discretion, proceed in the cause without making such persons parties; and in such cases the decree shall be without prejudice to the rights of the absent parties.

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No. 97-1732

IN THE
Supreme Court of the United States
OCTOBER TERM, 1998

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM and FLORIDA STATE BOARD OF ADMINISTRATION,
Petitioners,

v.

PAUL FELZEN, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

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REPLY BRIEF FOR PETITIONERS

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TABLE OF CONTENTS

	Page
TABLE OF AUTHORITIES	ii
ARGUMENT:	
A. This Court's Decisions Uphold the Rights of *De Facto* or *Quasi* Parties To Appeal	2
B. Respondents' Arguments for Denying Objecting Shareholders the Right To Appeal Are Unpersuasive and Reflect a Misunderstanding of Derivative Suits	8
C. The Policy Reasons Advanced by Respondents for Requiring Formal Intervention Are Unpersuasive	13
CONCLUSION	18

TABLE OF AUTHORITIES

CASES — Page

Bayard v. Lombard, 50 U.S. (9 How.) 530 (1850) 4
Bell Atlantic Corp. v. Bolger, 2 F.3d 1304 (3d Cir. 1993) 12, 13, 15, 16
Blossom v. Milwaukee R.R., 68 (1 Wall.) 655 (1864) 3, 10
Carlough v. Amchem Prods., Inc., 5 F.3d 707 (3d Cir. 1993) 12
Cement Antitrust Litig., In re, 688 F.2d 1297 (9th Cir. 1982), *aff'd sub nom. Arizona v. United States District Court*, 459 U.S. 1191 (1983) 12
Christian v. R. Hoe & Co., 63 F.2d 218 (2d Cir. 1933) 8
Clark v. Lomas & Nettleton Fin. Corp., 625 F.2d 49 (5th Cir. 1980), *cert. denied*, 450 U.S. 1029 (1981) 16
Ex parte Cockcroft, 104 U.S. 578 (1882) 4, 5
Cohen v. Young, 127 F.2d 721 (6th Cir. 1942) ..... *passim*
Connor v. Peugh's Lessee, 59 U.S. (18 How.) 394 (1855) 5
Ex parte Cutting, 94 U.S. 14 (1877) 4
Girsh v. Jepson, 521 F.2d 153 (3d Cir. 1975) 15
Gottlieb v. Wiles, 11 F.3d 1004 (10th Cir. 1993) 12, 13
Guthrie v. Evans, 815 F.2d 626 (11th Cir. 1987) 12
Hawes v. City of Oakland, 104 U.S. 450 (1881) 11
Johnson v. Manhattan Ry., 289 U.S. 479 (1933) 3, 8, 9
Karcher v. May, 484 U.S. 72 (1987) 4
Ex parte Leaf Tobacco Bd., 222 U.S. 578 (1911) 4
Marino v. Ortiz, 484 U.S. 301 (1988) 7, 9, 12
Marshall v. Holiday Magic, Inc., 550 F.2d 1173 (9th Cir. 1977) 12
PaineWebber Inc. Ltd. Partnerships Litig., In re, 94 F.3d 49 (2d Cir. 1996) 12
Payne v. Niles, 61 U.S. (20 How.) 219 (1857) 5
Pittsburgh & Lake Erie R.R. Sec. & Antitrust Litig., In re, 543 F.2d 1058 (3d Cir. 1976) 11
Rogers v. Consolidated Rock Prods. Co., 114 F.2d 108 (9th Cir. 1940) 6

TABLE OF AUTHORITIES—Continued

Page

Rosenbaum v. MacAllister, 64 F.3d 1439 (10th Cir. 1995) 15
Saylor v. Bastedo, 623 F.2d 230 (2d Cir. 1980) 15
Shults v. Champion Int'l Corp., 35 F.3d 1056 (6th Cir. 1994) 9
Smith v. Barry, 502 U.S. 244 (1992) 8
South St. Bldg. Corp., In re, 140 F.2d 363 (7th Cir. 1943), *cert. denied*, 322 U.S. 761 (1944) 5
Torres v. Oakland Scavenger Co., 487 U.S. 312 (1988) 7
Trust No. 2988, In re, 85 F.2d 942 (7th Cir.), *cert. denied*, 299 U.S. 609 (1936) 5
Tryforos v. Icarian Dev. Co., 518 F.2d 1258 (7th Cir. 1975), *cert. denied*, 423 U.S. 1091 (1976) 12
United States v. LTV Corp., 746 F.2d 51 (D.C. Cir. 1984) 4, 12
United States v. Seigel, 168 F.2d 143 (D.C. Cir. 1948) 4
United States Catholic Conference v. Abortion Rights Mobilization, Inc., 487 U.S. 72 (1988) 3
United States ex rel. Louisiana v. Jack, 244 U.S. 397 (1917) 4
West v. Radio-Keith-Orpheum Corp., 70 F.2d 621 (2d Cir. 1934) 3, 4
Wilkenson v. Hercules Engines, Inc., 138 F.3d 608 (6th Cir. 1998) 9
Williams v. Morgan, 111 U.S. 684 (1884) 3, 10

STATUTES AND RULES

Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, 109 Stat. 737 17
28 U.S.C. § 1291 7
Fed. R. App. P.:
Rule 1(b) 7
Rule 3(c) 7
Fed. R. Civ. P.:
Rule 23(c)(2)(C) 6
Rule 23(e) 12

TABLE OF AUTHORITIES—Continued

	Page
Rule 23.1	*passim*
Rule 24	2, 16

OTHER MATERIALS

Levi & Moore, *Federal Intervention II: The Procedure, Status, and Federal Jurisdictional Requirements*, 47 Yale L.J. 898 (1938)	5
15A Charles A. Wright, Arthur R. Miller & Mary Kay Kane, *Federal Practice and Procedure* (2d ed. 1992)	3, 13

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REPLY BRIEF FOR PETITIONERS

As petitioners and their *amici* established in their opening briefs, the Federal Rules are properly construed to permit an appeal by objecting shareholders in the circumstances presented here. Pursuant to Federal Rule of Civil Procedure 23.1, those objectors received notice and an opportunity to "show cause" why a proposed settlement should not be approved; they litigated their objections in district court; and the district court's approval of the settlement, if allowed to stand, will have claim preclusive effect on them. Permitting appeal in such circumstances comports with the decisions of this Court and many others allowing *de facto* or *quasi* parties to appeal without formal intervention. It also strongly furthers the clear legislative and judicial policy behind Rule 23.1—providing

federal courts with the information necessary to root out and deter insufficient and collusive derivative suit settlements.

Respondents complain that petitioners "are claiming a power suddenly to convert themselves into litigants by their own will—without any judicial scrutiny, without any opportunity for other parties to object, and without any district-court determination." ADM Br. 19. But the "power" they find so objectionable is precisely what is granted to all shareholders by Rule 23.1. Rule 23.1 specifically contemplates that objecting shareholders have the right to appear and present argument about whether a settlement should be approved—in respondents' words, to "convert themselves into litigants"—*without* formally intervening in the suit.

To be sure, by objecting to a settlement, shareholders do not become parties for all purposes. For that they would need to intervene pursuant to Rule 24—they then would have substantially greater rights (including the right to address other issues in the litigation) and would be subject to the scrutiny that respondents emphasize. But, under the Federal Rules, shareholders who only want to oppose the settlement need not undertake the burden of filing their own complaint, need not subject themselves to mandatory disclosure and discovery obligations, and need not convince the district court of their right to be heard. They are allowed to present their arguments in district court without undertaking such burdens in recognition of the fact that their rights as shareholders are necessarily adjudicated by any proposed settlement. And, if the district court rejects their objections to the settlement, they may make their case—on the same terms—in the court of appeals.

A. This Court's Decisions Uphold the Rights of *De Facto* or *Quasi* Parties To Appeal

1. Respondents spend a great deal of time defending the same simplistic, but plainly incorrect, proposition

adopted by the Seventh Circuit—that only parties may appeal. They claim that this Court has repeatedly held that "persons may not appeal the judgment of a federal court to which they have not been made or sought to become a party." ADM Br. 8-9; *see id.* at 15-26; ADM Directors Br. 22-24; Felzen Br. 8-10, 13-14.

But, in fact, this Court and many others have long held that persons who are not formal parties to the case but whose rights are necessarily being adjudicated *may* appeal. That is the teaching of *Johnson v. Manhattan Railway*, 289 U.S. 479 (1933), where the Court—consistent with centuries of common law precedent—concluded that shareholders who receive notice and present argument in district court are "entitled" to appeal a receivership ruling without intervening. *Id.* at 495 & n.4. It is also the teaching of *United States Catholic Conference v. Abortion Rights Mobilization, Inc.*, 487 U.S. 72, 76 (1988); *Williams v. Morgan*, 111 U.S. 684 (1884); *Blossom v. Milwaukee R.R.*, 68 U.S. (1 Wall.) 655 (1864), and the multitude of other cases cited in our opening brief and in the Solicitor General's *amicus* brief. *See* Pet. Br. 18-19, 24-27 & nn.21-26; Gov't Br. 7-11 & nn.1-4.

Thus, the rule allowing *de facto* or *quasi* parties to appeal is by no means a novel one; rather, it is moored in centuries of decisions rendered by this Court and many others. As Judge Learned Hand explained, while the general rule is that persons who are not formal parties may not appeal because their rights are "not concluded by the decree, and [they are] not therefore aggrieved by it," this Court's cases demonstrate that where a judgment "affects [that person's] interests, he is often allowed to appeal." *West v. Radio-Keith-Orpheum Corp.*, 70 F.2d 621, 624 (2d Cir. 1934) (citing, *inter alia, Blossom* and *Morgan*). *See also* 15A Charles A. Wright, Arthur R. Miller & Mary Kay Kane, *Federal Practice and Procedure* § 3902.1, at 122 (2d ed. 1992) ("Nonparties need not always go through a formal intervention procedure to achieve standing to appeal.").

Indeed, the very cases that ADM highlights (at 22) undermine its broad assertion. In *Karcher v. May*, 484 U.S. 72 (1987), the Court stated that the proposition that only formally admitted parties may appeal was a "*general rule*," not an exceptionless command. *Id.* at 77 (emphasis added). Both *Bayard v. Lombard*, 50 U.S. (9 How.) 530, 551 (1850), and *United States ex rel. Louisiana v. Jack*, 244 U.S. 397, 402 (1917) (citing *Ex parte Leaf Tobacco Bd.*, 222 U.S. 578 (1911)), state that the category of permissible appellants includes "*privies to the record*"—a class that has been determined to include shareholders that seek review of derivative suit settlements.[1] Other cases cited by respondents similarly confirm that the right to appeal extends to persons treated as parties by the trial court[2]—a category that, if it is to

[1] Relying on D.C. Circuit precedent (as well as other cases having nothing to do with which persons may appeal), ADM suggests (at 24) that the term "privies" refers only to successors to a property interest. But, in a more recent case that ADM ignores, the D.C. Circuit explicitly concluded that the *precise class of persons at issue here*—shareholders who object to derivative suit settlements—are "privies to the record" that may appeal because "judgments in such cases bind shareholders." *United States v. LTV Corp.*, 746 F.2d 51, 53-54 & n.5 (D.C. Cir. 1984).

Even in the D.C. Circuit case highlighted by ADM, *United States v. Seigel*, 168 F.2d 143 (D.C. Cir. 1948), the court of appeals discussed with approval Judge Learned Hand's earlier conclusion that a creditor who appeared to object to a receivership could appeal because, though not a formal party, "he was actually present and participating in the proceeding below after appearance upon notice duly given him." *Id.* at 145 (citing *West*, 70 F.2d at 623-24). That, of course, is precisely the case here. Moreover, the *Seigel* court approvingly quoted Judge Hand's decision in *West*: "'generally speaking no person, not a party to a suit, may appeal . . . [*b*]*ut if the decree affects his interests, he is often allowed to appeal.*'" *Id.* (quoting *West*, 70 F.2d at 623-24) (emphasis added). It is hard to imagine a statement that more directly undermines respondents' absolutist position.

[2] *Karcher*, 484 U.S. at 77; *Ex parte Cockcroft*, 104 U.S. 578, 578-79 (1882); *Ex parte Leaf Tobacco Bd.*, 222 U.S. 578, 578 (1911); *Ex parte Cutting*, 94 U.S. 14 (1877).

have meaning at all, must include persons who have received a legally mandated notice of court proceedings, who are entitled to present argument on that question before the trial court, and who will be subject to claim preclusion if a settlement is approved. *See* Pet. Br. 14-19; Gov't Br. 12-15.

Certainly, none of respondents' proffered cases involved persons whose rights were subject to claim preclusion once the case was decided and who were summoned to appear and show cause in trial court proceedings. *See, e.g., Ex parte Cockcroft*, 104 U.S. at 578 (denying appeal by party who "did not make it appear that he had any real interest in the controversy"); *Payne v. Niles*, 61 U.S. (20 How.) 219, 220 (1857) (person who had never sought relief directly against judgment debtor could not appeal judgment); *Connor v. Peugh's Lessee*, 59 U.S. (18 How.) 394, 395 (1855) (tenant who did not contest ejectment prior to judgment could not appeal).[3]

[3] Nor can law review articles plug this gaping hole in respondents' argument. Such articles, of course, cannot trump the decisions of this Court. In any event, the cited articles do not involve objectors under Rule 23.1, and they do not state the exceptionless rule respondents champion. Rather, as the language respondents quote suggests, they generally deal with particular circumstances involving, for instance, the rights of *amici curiae*. Respondents also twice cite Professors Levi and Moore for the statement that someone who "has not intervened, has no right of appeal." Levi & Moore, *Federal Intervention II: The Procedure, Status, and Federal Jurisdictional Requirements*, 47 Yale L.J. 898, 938 (1938). But the key case cited in that article, *In re Trust No. 2988*, 85 F.2d 942 (7th Cir.), *cert. denied*, 299 U.S. 609 (1936), involved an attempt by a bondholder to appeal on matters *other than those* as to which he was entitled to (and did) argue in district court. *See id.* at 943. That case has long been understood to be consistent with the proposition that *de facto* parties could appeal on issues that they were entitled to argue in the trial court. *See In re South St. Bldg. Corp.*, 140 F.2d 363, 367 (7th Cir. 1943) (distinguishing *Trust No. 2988* from instances where a stockholder or credit holder was a "party in interest" and "[f]ormal intervention was not required"

2. In the end, respondents are forced to abandon the absolutist proposition adopted by the Seventh Circuit. They acknowledge that some persons who are not formal parties may appeal.[4] Having discarded the Seventh Circuit's *reasoning*, however, respondents struggle to save its *result* with a series of newly minted limitations that, in their view, do not authorize objector appeals in this context.

For the reasons we discuss below, respondents' arguments on these points are no more persuasive than their primary submission. For now, however, the crucial point is that respondents' concession that some persons who are not formal parties may appeal fatally undermines their claims (*see* ADM Br. 18, 50) that this Court's cases mandate that *all* persons intervene before appealing and that a revision to the Federal Rules would be necessary to

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for purposes of appeal), *cert. denied*, 322 U.S. 761 (1944); *Rogers v. Consolidated Rock Prods. Co.*, 114 F.2d 108, 110 (9th Cir. 1940).

Professor Kaplan's footnote statement (cited at ADM Br. 14) about the right to appear and "receive papers" under Rule 23(c)(2)(C) says nothing about the right to be heard on settlements under Rule 23.1. His suggestion (cited at ADM Br. 16) about the inability of non-intervenors to "stop a settlement" by their disagreement says nothing about those persons' ability to object to a settlement in an effort to have a court disapprove it; and his statement about those persons' inability to appeal a case that has been *litigated* to judgment ("entered after contest") is notable for the fact that it does not speak to appeals from approved settlements.

[4] *See* ADM Directors Br. 34 (acknowledging cases where "non-parties with genuine, direct interests in the proceedings" were permitted to appeal); ADM Br. 30-36 (discussing appeals by *de facto* parties, by persons who are summoned or ordered, but are not parties, and by "disputants in ancillary proceedings"). The Felzen respondents purport to defend the proposition that only parties may appeal, but do so only by extending that term to include "non-formal" parties, a category that is functionally no different from the category that others have described as non-parties. *See* Felzen Br. 18.

permit appeals by *de facto* or *quasi* parties in this context.[5] Rather, intervention provides an *alternative* for persons who want the much greater rights associated with full party status—most basically, the right to be heard and to appeal on many issues *other* than the approval of the settlement. *Contrast* Felzen Br. 17 (wrongly suggesting that objectors want to be "super parties" with all the benefits of party status without any of the burdens).

Respondents' admission also fatally undermines any suggestion that *Marino v. Ortiz*, 484 U.S. 301 (1988), and/or Federal Rule of Appellate Procedure 3(c) absolutely bar all appeals by persons who are not parties.[6] The only question before the Court, therefore, is whether there is some *other* basis that the Seventh Circuit did not think of to support that court's conclusion that objecting shareholders may not appeal. As we now explain, there is not.

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[5] That concession also refutes the argument that this Court lacks jurisdiction over any petition that is not submitted by a formal party to the case. *See* ADM Br. 1. In any event, as the appellants in this matter, petitioners *were* parties to the court of appeals proceeding, even if they were not parties in the district court. Indeed, a rule that allowed persons to appeal to the court of appeals under 28 U.S.C. § 1291 (which, as we explained in our opening brief, never mentions party status), but precluded them from petitioning this Court would have the perverse effect of preventing the Court from serving its core function as the final arbiter of federal law.

[6] ADM's attempt (ADM Br. 19-21) to defend the Seventh Circuit's reliance on Rule 3(c) is thus ultimately beside the point. In any event, ADM never explains how the Seventh Circuit's understanding of that rule may be squared with Federal Rule of Appellate Procedure 1(b)'s statement that "[t]hese rules *shall not be construed to extend or limit the jurisdiction of the courts of appeals as established by law*" (emphasis added). *See* Pet. Br. 29. The decisions ADM quotes discuss only the need to comply with Rule 3(c)'s procedural requirements to invoke the court of appeals' jurisdiction; they do not purport to suggest that Rule 3(c) meant to, or does, limit the *kinds* of persons that may appeal. *See Torres v. Oakland Scavenger Co.*, 487 U.S. 312, 318 (1988) (holding that "et al." reference in notice of appeal did not provide sufficient indi-

B. Respondents' Arguments for Denying Objecting Shareholders the Right To Appeal Are Unpersuasive and Reflect a Misunderstanding of Derivative Suits

After grudgingly acknowledging that *some* persons who are not formal parties may appeal, respondents assert that shareholder objectors do not fall within the scope of the decisions permitting such appeals. Respondents proffer two primary distinctions between shareholder objectors and other *de facto* party appellants: (1) shareholder objectors are allegedly not "summoned" into court in the same way these other appellants are; and (2) shareholders do not have a sufficiently "direct" interest to support a right to appeal. Neither argument withstands scrutiny.

1. Respondents contend repeatedly that, unlike the *de-facto* parties that have been permitted to appeal, petitioners were not "summoned" or "haled into court." ADM Br. 26-27, 31-33; ADM Directors Br. 35-37; Felzen Br. 18-19. In fact, petitioners here are in precisely the same position as the appellants in *Manhattan Railway*, in *Christian v. R. Hoe & Co.*, 63 F.2d 218, 218 (2d Cir. 1933) (cited with approval in *Manhattan Railway* for permitting *de facto* party appeal), in *Cohen v. Young*, 127 F.2d 721, 724 (6th Cir. 1942), and in the other cases cited in our opening brief (at 21-22). In those cases, as here, appellants received a court notice informing them of the pendency of proceedings that affected their rights, that would subject them to claim preclusion, and that required them to appear to "show cause" *if they wished to be heard before the matter was finally adjudicated.* Respondents' suggestion that appellants in these cases were "compelled" to appear in some meaningfully different way than here is simply untenable. Respondents do not—and cannot—seriously claim that the corporate shareholder and bondholder appellants in *Manhattan Railway* and in *Christian*

cation that non-named party intended to appeal); *Smith v. Barry*, 502 U.S. 244, 245 (1992) (holding that document intended to serve as an appellate brief may qualify as a notice of appeal).

would have been hauled off by a Federal Marshal or held in contempt if they did not appear in court at the appointed time. In fact, the *Manhattan Railway* appellants did not appear in response to the court's "invit[ation]" to "show cause" (289 U.S. at 495), without any apparent consequence *except* the loss of their right to be heard on the relevant issue. *See id.*[7]

The full implausibility of respondents' argument is demonstrated by their attempts to distinguish *Cohen* on this ground. *See* ADM Br. 26.[8] In fact, *Cohen* involved the exact same situation as this case: the appellant was a shareholder objector who was notified under what is now Rule 23.1 to "show cause" why a derivative settlement should not be approved and who had appeared in district court to contest the settlement's fairness. *See* 127 F.2d at 724; Order Preliminarily Approving Settlement and Providing for Notice at 3 (May 30, 1997 (R.62)) (directing interested shareholders to "appear and show cause, if he, she or it has any [reason] why the proposed settlement of the derivative claims . . . should or should not be entered thereon").[9]

[7] Unable to come up with a legally relevant distinction for *Manhattan Railway*, respondents resort to labeling the case "unusual" (ADM Br. 22 n.22) and suggesting that the Court did not "focus[]" on the appellate jurisdiction issue (Felzen Br. 19). In fact, the Court addressed the relevant question and specifically cited cases that squarely authorized *de facto* party appeals *without intervention*. *See* 289 U.S. at 495 n.4.

[8] As respondents note, the Sixth Circuit itself has recently proffered this highly strained reading of *Cohen*. But the court's subsequent reading of that case was influenced by the same misinterpretation of *Marino* that infects respondents' briefs and the Seventh Circuit decision below and which we have shown cannot be squared with this Court's case law. *See Shults v. Champion Int'l Corp.*, 35 F.3d 1056, 1060-61 (6th Cir. 1994) (reading *Cohen* in light of an overly expansive understanding of *Marino*); *Wilkenson v. Hercules Engines, Inc.*, 138 F.3d 608, 611 (6th Cir. 1998) (applying *Shults*).

[9] Contrary to ADM's suggestion (ADM Br. 26), the fact that the appellant attempted to intervene played no part in the *Cohen* deci-

In sum, like petitioners here, the appellants in all these other cases were "haled into court" in the sense that the court alerted them that their rights would be finally adjudicated in their absence unless they appeared at the appointed time.

The fallacy in respondents' proffered distinction is further demonstrated by the fact that respondents acknowledge that situations exist where *de facto* parties are allowed to appeal even though they appeared in the trial court of their own volition—and thus could not conceivably have been "haled" into the matter. As the Solicitor General has explained in his *amicus* filing, cases such as *Blossom* (which involved bidders at a foreclosure sale) and *Williams* (which involved bondholders who had sought "leave to be heard" in the trial court as to certain trustee charges (111 U.S. at 693)) demonstrate that persons who have participated in the relevant trial court proceedings and whose rights are necessarily implicated by the order at issue may appeal as *quasi* parties, whether or not they have been "haled into" the proceeding against their will. *See* Gov't Br. 7-12.[10] Respondents similarly do not dispute that sureties that particiapte in district court proceedings may appeal in some instances even though they too appear purely on their own initiative. *See* Pet. Br. 26 & n.25.

2. Respondents ultimately retreat to a different, but equally untenable, distinction. They concede that "quasi

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sion. In fact, the court specifically stated that the failure to appeal the intervention denial was "not decisive" of appellant's right to appeal. 127 F.2d at 724.

[10] ADM suggests that these cases are distinct because they involved "ancillary proceedings." ADM Br. 33. The relevance of that distinction is elusive at best. The bidder appellant in *Blossom*, for instance, was surely not a formal party to the ancillary proceeding, and did not "subject itself to the jurisdiction" (*see id.* at 34) of the trial court to any greater extent than did petitioners here, who appeared at the time appointed by the district court to attempt to persuade the court as to how it should adjudicate their interests.

parties . . . with a direct financial interest in a proceeding" may appeal. ADM Directors Br. 39; *see* Felzen Br. 18. But, because a derivative suit recovers money for the corporation, not the individual shareholders, respondents reason that shareholders' interests in a derivative suit are not sufficiently "direct" to allow them to invoke the authority of an appellate court. *See* ADM Directors Br. 32-34; ADM Br. 25-26; Felzen Br. 15-17.

But the argument that shareholders lack a sufficiently concrete stake in derivative cases to invoke a federal court's authority simply second-guesses the judgment behind Rule 23.1. One might imagine a legal system in which shareholders' interests were understood to be too indirect to invoke a federal court's authority. But that is not our system. On the contrary, Rule 23.1, which largely codifies this Court's earlier decision in *Hawes v. City of Oakland*, 104 U.S. 450 (1881), represents an express judicial and legislative judgment that shareholders *are* sufficiently affected by harms to the corporation's interest that they may sue for a wrong done to the corporation. Accordingly, the question of the "directness" of a shareholder's interest has already been resolved—by this Court and by Congress in promulgating Rule 23.1. As the Solicitor General has explained, under Rule 23.1 "[o]wnership of the corporation's stock . . . gives both the objecting shareholder and the plaintiff shareholder a shared interest in the outcome of the case." Gov't Br. 13.

Moreover, as we have emphasized throughout, an objecting shareholder's direct and significant interest in the outcome of the litigation is demonstrated by the specific requirement that all shareholders be provided notice and an opportunity to be heard before a settlement is approved. It is precisely because a settlement would have claim preclusive effect on all shareholders' rights that the Federal Rules require that all shareholders be notified and permitted to present their arguments against a settlement during court proceedings. It is that same interest that permits them to appeal an adverse decision. *See, e.g., In re Pitts-*

burgh & Lake Erie R.R. Sec. & Antitrust Litig., 543 F.2d 1058, 1069-70 (3d Cir. 1976) (shareholders may appeal derivative suit since their "equity is being diluted"; their "distinctive interests are as worthy of consideration and protection as [party] shareholders"); *LTV Corp.*, 746 F.2d at 53-54 n.5 (objectors may appeal settlement approvals in derivative context because "judgments in such cases bind shareholders").[11]

Finally, respondents' emphasis on shareholders' supposed lack of a direct interest in the litigation is undermined by their own briefs. Respondents elsewhere stress that, "*a fortiori*," the decision in this case must apply in the class action context. ADM Br. 39-40. *See also* Pet. Br. 30 & n.29 (discussing the identity of language on objector rights in Rules 23(e) and 23.1). Yet even the Seventh Circuit conceded (Pet. App. 4a) that absent class members have a *direct* stake in the litigation. Accordingly, the alleged "indirectness" of shareholders' interests cannot provide a basis for resolving this case. *See also* 15A

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[11] ADM acknowledges that, before this case, *every* court of appeals to address this issue had concluded that shareholders may appeal without intervening. *See Cohen, supra*; *Tryforos v. Icarian Dev. Co.*, 518 F.2d 1258, 1263 n.22 (7th Cir. 1975) (Stevens, J.), *cert. denied*, 423 U.S. 1091 (1976); *Bell Atlantic Corp. v. Bolger*, 2 F.3d 1304 (3d Cir. 1993); *see also Gottlieb v. Wiles*, 11 F.3d 1004, 1011 (10th Cir. 1993). ADM argues, however, that the case law in the class action context is to the contrary. *See* ADM Br. 28-30. In fact, ADM ignores much case law recognizing the right to appeal in that context. *See, e.g., In re PaineWebber Inc. Ltd. Partnerships Litig.*, 94 F.3d 49, 53 (2d Cir. 1996); *Carlough v. Amchem Prods., Inc.*, 5 F.3d 707, 713-14 (3d Cir. 1993); *In re Cement Antitrust Litig.*, 688 F.2d 1297, 1309 (9th Cir. 1982), *aff'd sub nom. Arizona v. United States District Court*, 459 U.S. 1191 (1983); *Marshall v. Holiday Magic, Inc.*, 550 F.2d 1173, 1175 (9th Cir. 1977). And the cases ADM cites post-date and mistakenly rely upon *Marino* and *Guthrie v. Evans*, 815 F.2d 626, 628 (11th Cir. 1987). As one set of *amici* has explained, *Guthrie* did not even involve a settlement, and it has unfortunately led to incorrect decisions in a few circuit courts. *See* Brief *Amicus Curiae* of Public Citizen, Inc., *et al.*, at 11-17.

Wright, *et al., supra*, § 3902.1, at 129 ("[t]he determination whether to permit nonparty appeal does not rest alone on the directness . . . of the effects caused by an order").

C. The Policy Reasons Advanced by Respondents for Requiring Formal Intervention Are Unpersuasive

1. Respondents and their *amicus* do not dispute that in derivative litigation plaintiffs' counsel and defendants have strong incentives to settle for a small judgment and a large legal fee. Pet. Br. 13-14. They do not dispute that objecting shareholders help expose and prevent improper derivative settlements in the district court. Pet. Br. 32-33; WLF Br. 18 (citing additional authorities). They do not dispute that objecting shareholders serve this same function on appeal, providing strong incentive for district courts to take seriously shareholder objections and an avenue for correcting district court errors. Pet. Br. 33; WLF Br. 21-23 (citing additional authorities).

Instead, respondents deride these points as "policy arguments" that do not justify "rewriting" the plain language of the Federal Rules. ADM Br. 47-50; Felzen Br. 16-27. The unspoken premise of this argument, however, is that the text of the Federal Rules somehow *compels* intervention in all circumstances. Respondents have not produced —and cannot produce—a shred of support for such a conclusion. On the contrary, for all the reasons we have previously discussed, it is well-established that *de facto* parties may appeal without intervening.

Nor are respondents correct in deriding petitioners' points as mere "policy arguments." The federal courts charged with applying Rule 23.1 have themselves noted not only the absence of any statutory, regulatory, or constitutional impediment to objecting shareholder participation, but also the critical assistance objecting shareholders provide them in assessing the fairness and adequacy of derivative settlements. *See, e.g., Bell Atlantic*, 2 F.3d at 1310; *Gottlieb*, 11 F.3d at 1010-11; Pet. Br. 13-15 (citing additional authorities); Pet. 14-15 n.15 (same).

2. By contrast, it is respondents who manufacture "policy arguments" without any basis in Rule 23.1's language, history, or practice. They assert that requiring intervention will help deter the "proliferation" of appeals. Felzen Br. 23; ADM Br. 47. But the government, which bears responsibility in assisting in the administration and development of the Federal Rules, confirms that they "do not evince a concern that [the] limited degree of participation by persons other than the named plaintiff will unduly disrupt the litigation or render it unmanageable." Gov't Br. 28.

Respondents do not cite a single federal court that has ever claimed to be overworked by objecting shareholder appeals. In fact, petitioners have found just four reported objector appeals since 1990. Pet. Br. 37-38. ADM's own research reveals just 25 derivative settlement appeals during the 25-year period 1971-1996. ADM Br. 43. This is hardly evidence that the courts of appeals merit further insulation from a supposed tide of shareholder appeals. By contrast, respondents' rule would undeniably create additional work for overworked federal district courts by requiring them to resolve needless intervention motions. *See* Pet. Br. 38-39.

Respondents argue that requiring intervention would advance the social policy of "encouraging settlement." ADM Br. 45-46. None of respondents' arguments or authority, however, addresses settlement in the shareholder derivative suit context. In this peculiar arena, enormous and undisputed pressures *already* "encourage settlement"—even to the point of inducing collusive and improper deals. *See* Pet. Br. 13-14. Respondents cannot seriously argue (or cite any authority suggesting) that additional incentives to settlement are necessary or warranted. To the contrary, virtually every derivative suit brought today *is* settled. *See* Interview with Todd Foster, National Economic Research Associates (Dec. 21, 1998) (out of 371 derivative suits between 1975 and 1997, only five were

tried through verdict). Meanwhile, courts and commentators agree that further "hurdles" to objecting shareholder participation should be avoided in order to ensure courts sufficient adversarial information to assess the fairness of such deals. Pet. Br. 13-14 (citing authority); *Bell Atlantic*, 2 F.3d at 1310; *Cohen*, 127 F.2d at 725; WLF Br. 18-19 (citing further authority).[12]

Respondents chide us for lacking sufficient confidence in the trial courts to assess shareholders' objections without appellate oversight. Felzen Br. 25; ADM Br. 42. But respondents' own research reveals that reversals were obtained in fully 20 percent of derivative settlement appeals heard from 1971 through 1996. ADM Br. 43 (5 of 25 reversed).[13] This reversal rate parallels the national average

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[12] Felzen argues that the intervention requirement advances the related goal of providing "certainty as to when the litigation is over," noting that "[i]f no objector moves to intervene and the district court approves the settlement and enters judgment, the parties can be certain that the litigation is at an end." Felzen Br. 23. But the case is no more over if objecting shareholders appeal the denial of their intervention motions than if they appeal the denial of their objections to the settlement.

[13] ADM claims that of the five reversals, "only one rejected a settlement on the merits." *Id.* This is grossly misleading. In fact, each of these cases illustrates why access to the courts of appeals is essential. Courts variously reversed in these cases because the proposed attorney fees were too high; the parties' proposed settlement was too low; the fairness of the settlement was impossible to determine because the trial court had impermissibly silenced objecting shareholders; or there was compelling evidence of director collusion. *See Rosenbaum v. MacAllister*, 64 F.3d 1439, 1448 (10th Cir. 1995) (remanding $2.6 million attorney fee award, which trial court later reduced by $1.4 million, *see* Pet. Br. 33); *Saylor v. Bastedo*, 623 F.2d 230, 232-33 (2d Cir. 1980) (Friendly, J.) (court ordered reconsideration of settlement earmarking $250,000 for attorney fees and just $57,000 for stockholders when claim had a face value of "many millions" that had "sufficient support . . . to prompt this court to observe that 'plaintiff was not far from making a *prima facie* case' "); *Girsh v. Jepson*, 521 F.2d 153, 156-60 (3d Cir. 1975) (remanding because trial court denied objecting

for all civil cases, underscoring that appellate review and error correction is as warranted here as in any civil setting. Pet. Br. 33 (reporting civil reversal rates of between 16 and 27 percent). It is hardly an indictment of federal trial courts to acknowledge that some improper settlements may evade their detection; the Third Circuit has itself expressly worried about just this possibility. *Bell Atlantic*, 2 F.3d at 1310.

3. Nor is there any doubt that under respondents' rule objecting shareholders would be effectively barred from appealing. Respondents abandon their prior intimations that the Court should rewrite Rule 24 to make shareholder intervention easy and costless.[14] Nowhere in their briefs do they dispute that objecting shareholders' motions to intervene would have a hard time meeting Rule 24's "timeliness" and "adequate representation" tests. Pet. Br. 34-35. To the contrary, ADM offers only the cold comfort that objecting shareholders could bring separate lawsuits against company directors when they can prove outright fraud by the parties in the original derivative litigation. ADM Br. 45. Felzen similarly notes only that objectors would be able to appeal denials of intervention. Felzen Br. 26. Such an appeal would, however, be a fruitless formalism if any intervention motion could be properly denied under Rule 24 as respondents now suggest.[15]

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shareholders participation and, as a result, court lacked sufficient information to assess settlement's fairness); *Clark v. Lomas & Nettleton Fin. Corp.*, 625 F.2d 49 (5th Cir. 1980) (vacating and remanding where evidence suggested directors collusively settled suit), *cert. denied*, 450 U.S. 1029 (1981).

[14] *Compare* ADM Br. in Opp. 16 *and* ADM Directors' Br. in Opp. 14-15 *with* ADM Br. 18 (arguing compliance with Rule 24 should not be "an empty formality").

[15] Felzen dismisses petitioners' "fear of discovery" as mere "speculation." Felzen Br. 26. But the practical disincentives associated with intervening are wholly beside the point if (as respondents no longer contest) any intervention motion would be denied as a matter of law. Pet. Br. 34-35. Besides, members of the judiciary have recognized that the practical disincentives associated with accepting discovery obligations can be staggering even for large institutional investors. *See* Pet. Br. 35-36 (quoting District Judge Vaughn R. Walker). To take but one recent example, as soon as the Wisconsin Investment Board assumed the "lead plaintiff" role in a recent securities fraud class action pursuant to the Private Securities Litigation Reform Act of 1995 it was immediately pummeled with irrelevant and harassing demands for all documents concerning the performance of its investments and for depositions of its officers. *See Gluck v. Cellstar Corp.*, No. 3:96-CV-1353-R (N.D. Tex.).

In the end, respondents would have the Court chase the policy goal of "encouraging settlement" in an arena where virtually all cases already settle—even if it means extinguishing appeals by objecting shareholders whose rights are directly affected and finally adjudicated, insulating many derivative suit settlements from federal appellate court review designed to ensure that they are not insufficient or even the product of collusion, tolerating an error rate of 20 percent or more, and imposing a new round of motion practice on busy federal district courts. Nothing in the Constitution, federal statutes, or the Federal Rules of Civil Procedure supports such a result, and both this Court's cases and common law tradition point in exactly the opposite direction.

CONCLUSION

The Seventh Circuit's order dismissing petitioners' appeal should be reversed.

Respectfully submitted,

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CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM, ET AL., PETITIONERS

v.

PAUL FELZEN, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE UNITED STATES AND THE SECURITIES AND EXCHANGE COMMISSION AS AMICI CURIAE SUPPORTING PETITIONERS

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QUESTION PRESENTED

Whether a shareholder who is not a named plaintiff but who submits an objection to a proposed settlement in a derivative action in district court, in response to notice provided under Federal Rule of Civil Procedure 23.1, may appeal the approval of the settlement without formally intervening as a party.

TABLE OF CONTENTS

	Page
Interest of the Amici	1
Statement	2
Summary of argument	4
Argument:	
Objecting shareholders may appeal an order approving a settlement in a shareholder derivative suit	5
A. The right of objecting shareholders to appeal is longstanding and grounded in this Court's cases involving quasi parties	5
B. Upholding the rights of objecting shareholders to appeal district court decisions approving settlements furthers the purposes underlying the rule	19
C. The court of appeals' contrary reasoning is unpersuasive	24
Conclusion	29

TABLE OF AUTHORITIES

Cases:

Aetna Life Ins. Co. v. *Alla Medical Servs.*, 855 F.2d 1470 (9th Cir. 1988)	27
Alleghany Corp. v. *Kirby*, 333 F.2d 327 (2d Cir. 1964), cert. dismissed, 384 U.S. 933 (1965)	23
American Pipe & Constr. Co. v. *Utah*, 414 U.S. 538 (1974)	25
Baldwin v. *Hale*, 68 U.S. (1 Wall.) 223 (1864)	15
Bateman Eichler, Hill Richards, Inc. v. *Berner*, 472 U.S. 299 (1985)	1
Bayard v. *Lombard*, 50 U.S. (9 How.) 530 (1850)	11, 27
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Cases—Continued: Page

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Blake v. *District Court*, 59 F.2d 78 (9th Cir. 1932) 8
Blossom v. *The Milwaukee Railroad*, 68 U.S. 655 (1 Wall.) (1863) 4, 8, 9, 10, 11, 17
Blue Chip Stamps v. *Manor Drug Stores*, 421 U.S. 723 (1975) 1
Boggess v. *Hogan*, 410 F. Supp. 433 (N.D. Ill. 1976) 21
Brand Name Prescription Drugs Antitrust Litigation, In re, 115 F.3d 456 (7th Cir. 1997), cert. denied, 118 S. Ct. 1178 (1998) 4
Bryant v. *Yellin*, 447 U.S. 352 (1980) 29
Christian v. *R. Hoe & Co.*, 63 F.2d 218 (2d Cir. 1933) 8
Cockcroft, Ex parte, 104 U.S. 578 (1881) 11
Cohen v. *Beneficial Indus. Loan Corp.*, 337 U.S. 541 (1949) 13, 14
Cohen v. *Young*, 127 F.2d 721 (6th Cir. 1942) 5, 6, 7, 12, 23, 24
Collier v. *Marshall, Dennehey, Warner, Coleman & Goggin*, 977 F.2d 93 (3d Cir. 1992), cert. denied, 510 U.S. 977 (1993) 18, 27
Cutting, Ex parte, 94 U.S. 14 (1876) 12
Daily Income Fund, Inc. v. *Fox*, 464 U.S. 523 (1984) 13
Davis v. *Mercantile Trust Co.*, 152 U.S. 590 (1894) 17
DeLuca v. *Long Island Lighting Co.*, 862 F.2d 427 (2d Cir. 1988) 27
Eisen v. *Carlisle & Jacquelin*, 417 U.S. 156 (1974) 15
Ford v. *Douglas*, 46 U.S. 143 (1847) 12

Cases—Continued: Page

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Granada Invs., Inc. v. *DWG Corp.*, 962 F.2d 1203 (6th Cir. 1992) 22
Greenspun v. *Bogan*, 492 F.2d 375 (1st. Cir. 1974) 21, 22
Guthrie v. *Evans*, 815 F.2d 626 (11th Cir. 1987) 25
Hawes v. *City of Oakland*, 104 U.S. 450 (1881) 13
Hinckley v. *Gilman, Clinton & Springfield R.R.*, 94 U.S. 467 (1876) 8-9, 10
Hovey v. *McDonald*, 109 U.S. 150 (1883) 10
Indiana S. R.R. Liverpool, London & Globe Ins. Co., 109 U.S. 168 (1883) 11
J.I. Case Co. v. *Borak*, 377 U.S. 426 (1964) 1
Jiffy Lube Securities Litig., In re, 927 F.2d 155 (4th Cir. 1991) 22
Johnson v. *Manhattan Ry.*, 289 U.S. 479 (1933) 7, 8
Jones v. *Nuclear Pharmacy, Inc.*, 741 F.2d 322 (10th Cir. 1984) 15, 22
Kneeland v. *American Loan & Trust Co.*, 136 U.S. 89 (1890) 8, 16
Litchfield v. *Goodnow*, 123 U.S. 549 (1887) 11
Maher v. *Zapata*, 714 F.2d 436 (5th Cir. 1983) 14, 15, 21
Marino v. *Ortiz*, 484 U.S. 301 (1988) 3, 5, 12, 25, 26, 27
Martin v. *Wilks*, 490 U.S. 755 (1989) 26
Massachusetts School of Law at Andover, Inc. v. *United States*, 118 F.3d 776 (D.C. Cir. 1997) 18
Matsushita Elec. Indus. Co. v. *Epstein*, 516 U.S. 367 (1996) 14-15
Miltier v. *Downes*, 935 F.2d 660 (4th Cir. 1991) 27
Minnesota Co. v. *St. Paul Co.*, 69 U.S. (2 Wall.) 609 (1864) 10, 11

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Mitchell v. *Lay*, 48 F.2d 79 (9th Cir. 1930) 8
Mokhiber v. *Cohn*, 783 F.2d 26 (2d Cir. 1986) 27-28
Mylett v. *Jeane*, 879 F.2d 1272 (5th Cir. 1989) 22
National Student Marketing Litig., In re, 68 F.R.D. 151 (D.D.C. 1974) 21
Pacific Enterprises Sec. Litig., In re, 47 F.3d 373 (9th Cir. 1995) 28
Pianta v. *H.M. Reich Co.*, 77 F.2d 888 (2d Cir. 1935) 7
Papilsky v. *Berndt*, 466 F.2d 251 (2d Cir.), cert. denied, 409 U.S. 1077 (1972) 23
Phillips Petroleum Co. v. *Shutts*, 472 U.S. 797 (1985) 15
Reynolds v. *National Football League*, 584 F.2d 280 (8th Cir. 1978) .....
Sage v. *Railroad Co.*, 96 U.S. 712 (1877) 10, 17
Saylor v. *Lindsley*, 456 F.2d 896 (2d Cir. 1972) 21
Shelton v. *Pargo, Inc.*, 582 F.2d 1298 (4th Cir. 1978) .....
Stacy v. *Thrasher*, 47 U.S. 44 (1848) 12
Trustees v. *Greenough*, 105 U.S. 527 (1881) 10, 17
Tryforos v. *Icarian Development Co.*, 518 F.2d 1258 (7th Cir. 1975), cert. denied, 423 U.S. 1091 (1976) 5
United Airlines, Inc. v. *McDonald*, 432 U.S. 385 (1977) 27
United States v. *LTV Corp.*, 746 F.2d 51 (D.C. Cir. 1984) 18
United States v. *Seigel*, 168 F.2d 143 (D.C. Cir. 1948) 9
United States ex rel. Louisiana v. *Jack*, 244 U.S. 397 (1917) 26, 27

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Webster Coal & Coke Co. v. *Cassatt*, 207 U.S. 181 (1907) 19
West v. *Radio-Keith-Orpheum Corp.*, 70 F.2d 621 (2d Cir. 1934) 8
West v. *Randall*, 29 F. Cas. 718 (C.C.D.R.I. 1820) (No. 17,424) 11
White v. *Auerbach*, 500 F.2d 822 (2d Cir. 1974) 21
Williams v. *Morgan*, 111 U.S. 684 (1884) 4, 8, 10, 17

Statutes, regulation, and rules:

Antitrust Penalties and Procedure Act, 15 U.S.C. 16(b)-(h) 18
Comprehensive Environmental Response, Compensation and Liability Act of 1980, 42 U.S.C. 9601 *et seq.*:
42 U.S.C. 9613(i) 19
42 U.S.C. 9622(d)(2) 19
Solid Waste Disposal Act, 42 U.S.C. 3251 *et seq.*:
42 U.S.C. 6972(b)(1) 19
42 U.S.C. 6972(b)(2)(E) 19
42 U.S.C. 6973(d) 19
15 U.S.C. 4 18
15 U.S.C. 15 18
15 U.S.C. 16(f)(3) 18
15 U.S.C. 25 18
15 U.S.C. 26 18
42 U.S.C. 2000e 26
42 U.S.C. 2000e-2(a) 26
28 C.F.R. 50.7 19
Fed. R. App. P.:
Rule 3(c) 3, 5, 27, 28
Rule 3(c)(3) 28
Fed. R. Civ. P.:
Rule 23 ..... 4, 7, 19, 20, 21
Rule 23(c) 21

Rules—Continued:	Page
Rule 23.1	*passim*
Rule 23.1(1)	13
Rule 24	24
Miscellaneous:	
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J. Moore & E. Levi, *Federal Intervention, Part I: The Right to Intervene and Reorganization*, 45 Yale L.J. 565 (1936)	7
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5 *Moore's Federal Practice* (D. Coquillette et al. eds., 3d ed. 1997)	13, 14
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In the Supreme Court of the United States

OCTOBER TERM, 1998

No. 97-1732

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM, ET AL., PETITIONERS

v.

PAUL FELZEN, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE UNITED STATES AND THE SECURITIES AND EXCHANGE COMMISSION AS AMICI CURIAE SUPPORTING PETITIONERS

INTEREST OF THE AMICI

This case presents an issue of importance to the management and disposition of shareholder derivative actions, which may involve claims under the federal securities laws and issues of corporate governance of critical importance to shareholders. The Securities and Exchange Commission (SEC) has long taken the view that private actions under the federal securities laws serve important functions, in compensating investors who have been harmed by securities law violations and providing "'a most effective weapon in the enforcement' of the securities laws, and are 'a necessary supplement to [SEC] action.'" *Bateman Eichler, Hill Richards, Inc.* v. *Berner*, 472 U.S. 299, 310 (1985) (quoting *J.I. Case Co.* v. *Borak*, 377 U.S. 426, 432 (1964)); see also *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 730 (1975).

The SEC also has an interest in protecting investors through effective corporate governance. The federal government more generally has a substantial interest in the procedural rules that apply in class action suits in a variety of contexts.

STATEMENT

1. On October 15, 1996, Archer Daniels Midland Corporation (ADM) pleaded guilty to federal criminal antitrust violations involving charges that company officers had conspired to fix the price of citric acid. The company paid a $100 million fine and subsequently settled civil antitrust lawsuits filed by competitors for $90 million. Pet. 4.

In the wake of the criminal investigation, ADM shareholders filed several derivative actions on behalf of ADM against directors of the corporation. Those actions were consolidated in United States District Court for the Central District of Illinois. The suits alleged that the directors had breached their fiduciary duties by failing to supervise company employees properly and sought recovery of the $190 million paid out in the criminal and private cases. Pet. 4-5.

On May 29, 1997, the parties in the consolidated cases announced a proposed settlement pursuant to which the shareholders would release the defendants from all claims in exchange for a settlement fund of $8 million (Felzen Br. in Opp. App. 2) and the adoption of corporate governance reforms (ADM Br. in Opp. App. 13a-15a) designed to prevent similar violations in the future. Of the $8 million amount, $3.92 million, plus interest, was to be paid to plaintiffs' counsel (Pet. App. 17a), with the remaining amount designated for legal fees incurred by ADM in adopting agreed-upon reforms (Pet. 6). Neither the corporation nor its shareholders would receive any monetary recovery from the settlement.

2. The district court tentatively approved the settlement on May 30, 1997. Pet. 7. Pursuant to Federal Rule of Civil Procedure 23.1, the court ordered that notice be given to all

ADM shareholders to show cause why the settlement should not be approved. The court ordered that all objections were to be filed by July 3, 1997, and scheduled a final hearing on the settlement for July 7, 1997. Pet. 7. Petitioners California Public Employees' Retirement System and the Florida Board State Board of Administrtion—which hold, respectively, 2.8 million and 1.7 million shares of ADM stock—filed written objections with the district court and appeared at the July 7 hearing. ADM Br. in Opp. App. 4a; Pet. 7. They argued that the settlement disproportionately benefited the plaintiffs' lawyers and that the corporate governance reforms agreed to were not materially better than reforms adopted by ADM a year earlier. ADM Br. in Opp. App. 15a. The district court approved the settlement over petitioners' objections. Felzen Br. in Opp. App. 1-7.

3. The court of appeals dismissed petitioners' appeal, reasoning that, since petitioners had not moved to intervene for purposes of taking an appeal, they were not parties to the case. Pet. App. 3a. The court of appeals held that, under this Court's decision in *Marino* v. *Ortiz*, 484 U.S. 301, 304 (1988), only parties may take an appeal. Pet. App. 1a-2a. The court read *Marino* (a class action rather than a derivative suit) to hold "that a person adversely affected by the settlement of a class action may appeal from the consent decree based on that settlement only if he has intervened as a party." *Id.* at 2a. The court also noted that Federal Rule of Appellate Procedure 3(c) specifies that "[a] notice of appeal must specify the *party or parties* taking the appeal by naming each appellant in either the caption or the body of the notice of appeal." *Ibid.*

The court observed that prior to *Marino* it had "permitted class members and stockholders to appeal, whether or not they had intervened, provided they had informed the district court of their objections to the decision that disadvantaged them." Pet. App. 2a. But it further noted that since *Marino* it had "held that a class member in an action under Fed. R.

Civ. P. 23 who has not become a party may not appeal from an order granting summary judgment to the defendant." *Ibid.* (citing *In re Brand Name Prescription Drugs Antitrust Litigation*, 115 F.3d 456 (7th Cir. 1997)). The court reasoned that the same rule should apply to shareholders in a derivative suit challenging a settlement, because shareholders "have no more right to speak for the firm or control its litigation decisions than bondholders or banks or landlords, all of whom have contractual interests that may be affected by litigation." Pet. App. 3a. Although the court recognized that Rule 23.1 requires that shareholders be given notice of the settlement, it read the purpose of that requirement to be "so that other investors may contest the faithfulness or honesty of the self-appointed plaintiffs; we do not doubt that this monitoring is often useful and that intervention to facilitate an appeal could be justified." Pet. App. 6a.

SUMMARY OF ARGUMENT

Until the decision below, courts had uniformly held that objecting shareholders in a derivative action had the limited right to appeal the district court's entry of a settlement decree without formally intervening in the suit. That rule finds support in this Court's cases involving certain persons deemed to be "quasi parties," who have been summoned to court or to whom notice of proceedings has been directed, who appear in court to protect particular interests, and whose rights are affected by claim preclusion principles by the court's judgment. See, *e.g.*, *Williams* v. *Morgan*, 111 U.S. 684 (1884); *Blossom* v. *The Milwaukee R.R.*, 68 U.S. (1 Wall.) 655 (1863). That line of cases, coupled with the procedures of and the purposes behind Federal Rule of Civil Procedure 23.1, support the limited right of objecting shareholders to appeal the court's decree overruling their objections and approving the settlement. Rule 23.1 requires directed notice to all shareholders so that any objector to a

settlement may show cause why the settlement should not be approved. The court's entry of a settlement decree has claim preclusive effect, extinguishing the right of the corporation and the shareholders thereafter to bring the same claim.

The decision below erred in its reliance on *Marino* v. *Ortiz*, 484 U.S. 301 (1988), which involved an attempt to appeal in a class action suit by non-parties who were not members of the class. In *Marino*, the appellants were strangers to the litigation and were not precluded by the judgment from subsequently litigating their claims. The court also erred in relying on Federal Rule of Appellate Procedure 3(c), which defines the contents of the notice of appeal and does not specify that the "party or parties" taking the appeal must be limited to the party or parties who were formally named in the district court proceedings.

ARGUMENT

OBJECTING SHAREHOLDERS MAY APPEAL AN ORDER APPROVING A SETTLEMENT IN A DERIVATIVE SUIT

A. The Right Of Objecting Shareholders To Appeal Is Longstanding And Grounded In This Court's Cases Involving Quasi Parties

In overruling one of its prior decisions, the Seventh Circuit departed from a uniform rule in derivative actions that had long been applied in the courts of appeals permitting an objecting shareholder to appeal without formal intervention if the district court overruled the shareholder's objections in entering a settlement decree. See *Bell Atlantic Corp.* v. *Bolger*, 2 F.3d 1304, 1308 n.6 (3d Cir. 1993); *Tryforos* v. *Icarian Development Co.*, 518 F.2d 1258, 1263 n.22 (7th Cir. 1975) (Stevens, J.), cert. denied, 423 U.S. 1091 (1976), overruled by Pet. App. 7a; *Cohen* v. *Young*, 127 F.2d 721 (6th Cir. 1942). That rule had been reported by influential

commentators without any question as to its validity. See, *e.g.*, 7C C. Wright et al., *Federal Practice & Procedure* § 1839, at 182 (2d ed. 1986) ("[a]n objector to the settlement may appeal the court's approval of the compromise"); 3B J. Moore, 5 *Moore's Federal Practice* ¶ 23.1.24[3] (2d ed. 1996) (same). Indeed, one commentator wrote in 1969 that "[i]f the court approves the compromise [between plaintiff-shareholders and defendants], the objector has an absolute right to appeal." W. Haudek, *The Settlement and Dismissal of Shareholders' Actions–Part II: The Settlement*, 23 SW. L.J. 765, 803 (1969). Although the rule was widely accepted, its origins and underlying legal basis appear to have been forgotten.

1. The modern application of the rule that objecting shareholders may appeal an order approving a settlement to which they object stems from the Sixth Circuit's decision in *Cohen* v. *Young*, *supra*. That case, which was decided shortly after promulgation of the Federal Rules of Civil Procedure, involved a shareholder in a derivative action who brought forward evidence in support of his objection to a proposed settlement, along with a motion to intervene as a party. The district court denied the objector's intervention motion and refused to consider the evidence proffered in support of the objection. The objecting shareholder did not appeal the denial of his motion to intervene, but rather appealed from the district court's entry of a final decree approving the settlement. On appeal, the plaintiff shareholder moved to dismiss on "the ground that appellant is not a party to this cause and hence has no standing in this court." 127 F.2d at 724. The court of appeals deemed "not decisive" the fact that the objecting shareholder had been denied the right to intervene. "Appellant appeared in court in answer to the court's notice to show cause why the settlement should not be approved. This being the case, he was 'like a defendant who is summoned by process of court and after an adverse ruling has the right to appeal.'" *Ibid.* In reaching

that conclusion, the court noted that "[t]his ruling was specifically approved in *Johnson* v. *Manhattan Ry. Co.*, 289 U.S. 479, 495. Appellant is entitled as of right to prosecute the appeal." *Ibid.* (parallel citations omitted).[1]

The *Cohen* court thus reasoned that because Federal Rule of Civil Procedure 23 created a specific mechanism for directed notice to all shareholders that they could appear in the district court proceedings for the limited purpose of showing cause why the proposed settlement should not be approved, the objecting shareholder became a "party" for that limited purpose. 127 F.2d at 724. The requirement of formal intervention under Rule 24 did not speak to the question raised by the shareholder's objection, which was "whether the compromise recommended did in fact protect the interest of the corporation and of the stockholders." *Id.* at 725. See also J. Moore & E. Levi, *Federal Intervention, Part I: The Right to Intervene and Reorganization*, 45 Yale L.J. 565, 592 (1936) (noting that a stockholder typically cannot intervene in a lawsuit because litigation decisions are controlled by the directors and officers of the corporation).

2. The *Cohen* court appropriately drew from this Court's analogous decision in *Johnson*. In that case, the Court addressed whether a separate shareholder derivative suit could be brought by a minority shareholder on behalf of a company that, in a prior non-derivative suit, had been the subject of an order appointing a temporary receiver. The object of the minority shareholder's subsequent suit was also the appointment of a receiver. In ruling that the minority shareholder and another plaintiff could not bring that suit,

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[1] *Cohen* also cited *Pianta* v. *H.M. Reich Co.*, 77 F.2d 888, 890 (2d Cir. 1935), in which the court found "no merit in appellees' contention that the appellant has no standing to appeal because it was not an original party to the suit and has not sought to intervene. The appellant, having appeared in opposition to the order to show cause, is 'like a defendant who is summoned by process of court and after an adverse ruling has the right to appeal.'"

the Court noted that both had been ordered in the prior proceeding to show cause "why the temporary receivership should not be continued." 289 U.S. at 495. They could have objected on a variety of grounds, "and had the receivership been continued without giving effect to these objections they would have been entitled to appeal." *Ibid.* Although the Court cited as support for that conclusion a number of court of appeals decisions, see *ibid.* n.4,[2] it could as easily have relied upon numerous of its own prior decisions that the courts of appeals had cited, which permitted limited appeals in discrete circumstances by certain "quasi parties" to the underlying lawsuit.[3]

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[2] In particular, see *Christian* v. *R. Hoe & Co.*, 63 F.2d 218, 218 (2d Cir. 1933) (upholding appeal of a "class A stockholder who appeared on the return day of the order to show cause why the receivership of the defendant should not be made permanent. He opposed the application unsuccessfully and appeals. He is rightfully here, like a defendant who is summoned by process of court and after an adverse ruling has the right to appeal."); *Mitchell* v. *Lay*, 48 F.2d 79, 84-85 (9th Cir. 1930) ("It is true that the appellant is not a party to the original action, but when he was brought into court by the process of the court at the instigation of the parties to the action or of the receiver he became a party to the ancillary proceedings and entitled to appeal from the judgment rendered against him. The judgment therein rendered was as to him final and appealable as such."); see also *Blake* v. *District Court*, 59 F.2d 78, 79 (9th Cir. 1932) (holding that a person aggrieved by appointment of receiver should file objections in the district court and then appeal an adverse decision rather than petition for an original writ in the court of appeals).

[3] Although the phrase "quasi parties" typically was not utilized by mid-twentieth century courts in the shareholder and receiver contexts, the holdings of the later courts relied on this Court's decisions from the nineteenth and early twentieth centuries establishing rights of appeal for persons termed "quasi parties" in particular actions analogous to shareholder derivative suits. See, *e.g.*, *West* v. *Radio-Keith-Orpheum Corp.*, 70 F.2d 621, 623-624 (2d Cir. 1934) (L. Hand, J.) (citing *Blossom* v. *The Milwaukee R.R.*, 68 U.S. (1 Wall.) 655 (1863); *Williams* v. *Morgan*, 111 U.S. 684 (1884); *Kneeland* v. *American Loan & Trust Co.*, 136 U.S. 89 (1890)); *Christian*, 63 F.2d at 218 (citing *Hinckley* v. *Gilman, Clinton &*

In *Blossom* v. *The Milwaukee Railroad*, 68 U.S. (1 Wall.) 655 (1863), for example, the Court addressed the issue, "Is the appellant so far a party to the original suit that he can appeal?" *Id.* at 655. In that case Blossom had made a bid for property in response to a decree foreclosing a mortgage and ordering a sale. The sale was suspended and Blossom sought to have the sale completed and confirmed. After the district court refused his request, he appealed. The railroad moved to dismiss the appeal on the ground that Blossom was not a party to the suit in the district court and therefore not entitled to prosecute an appeal. This Court rejected the railroad's argument and upheld Blossom's appeal. In a passage that would be much quoted and cited in later decisions, the Court explained:

> It is certainly true that [Blossom] cannot appeal from the original decree of foreclosure, nor from any other order or decree of the court made prior to his bid. It, however, seems to be well settled, that after a decree adjudicating certain rights between the parties to a suit, other persons having no previous interest in the litigation may become connected with the case, in the course of subsequent proceedings, in such a manner as to subject them to the jurisdiction of the court, and render them liable to its orders; and that they may in like manner acquire rights in regard to the subject-matter of the litigation, which the court is bound to protect. Sureties, signing appeal bonds, stay bonds, delivery bonds, and receipters under writs of attachment, become *quasi* parties to the proceedings, and subject themselves to the jurisdiction of the court, so that summary judgments

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Springfield R.R., 94 U.S. 467 (1876)). See also *United States* v. *Seigel*, 168 F.2d 143, 145-146 (D.C. Cir. 1948) (distinguishing Supreme Court quasi party cases because appellant had not participated in district court proceedings and thus had no basis for appealing without formally intervening as a party).

> may be rendered on their bonds or recognizances. So in the case of a creditor's bill, or other suit, by which a fund is to be distributed to parties, some of whom are not before the court; these are at liberty to come before the master after the decree, and establish their claims to share in the distribution.

Id. at 655-656.

Blossom was not an anomalous decision. In *Williams* v. *Morgan*, 111 U.S. 684 (1884), the Court held that objectors to trustee charges were "quasi parties" entitled to appeal an adverse decision without formally intervening through the filing of a complaint: "Williams and Thomson had such an interest [in the trustee charges], and were so situated in the cause, that they had a right, by leave of the court, to except and object to the charges and allowances presented by the trustees and receivers, and that they had a right to appeal from the decree of the Circuit Court to this court." 111 U.S. at 700. As support for that holding, the Court drew on a line of cases starting with *Blossom* that had upheld the right of quasi parties "to come into this court, or to be brought here on appeal, when a final decision of their right or claim has been made by the court below." *Id.* at 699.[4] The Court also

[4] See *Blossom*, 68 U.S. (1 Wall.) at 656 (purchaser of property subject to foreclosure decree permitted to appeal as a quasi party); *Minnesota Co.* v. *St. Paul Co.*, 69 U.S. (2 Wall.) 609, 633-634 (1864) (holding that "nominal parties" could not evade appellate review of an order decreed in their favor on the ground that they were not formal parties in the district court); *Hinckley*, 94 U.S. at 469 (receiver allowed to appeal from a decree against him to pay a sum of money in the cause to which he was appointed receiver but was not a party); *Sage* v. *Railroad Co.*, 96 U.S. 712, 714 (1877) (quasi parties interested in order confirming a sale permitted to appeal); *Trustees* v. *Greenough*, 105 U.S. 527, 531 (1881) (allowing appeal by trustees from an order awarding costs and expenses to a complainant suing on behalf of a trust fund); *Hovey* v. *McDonald*, 109 U.S. 150, 155-156 (1883) (permitting appeal to be brought against a receiver from an order made in his favor notwithstanding receiver's contention that he was not a "party" to the underlying lawsuit).

relied upon principles of equity that recognized the rights and interests of quasi parties to participate in trial proceedings without formal intervention and to appeal decisions that would bind their subsequent rights.[5] Decades earlier, Justice Story had recognized the rights of class members in representative suits to appear in court "as quasi parties to the record, at least for the purpose of taking the benefit of the decree, and of entitling themselves to other equitable relief, if their rights are jeoparded." *West* v. *Randall*, 29 F. Cas. 718, 722-723 (C.C.D.R.I. 1820) (No. 17,424). See also J. Story, *Commentaries on Equity Pleadings* § 409, at 353 (9th ed. 1879) (noting that "other persons in interest" who are not parties may bring a bill of review "as far as their own interests are concerned"). Thus, as the doctrine of quasi parties developed, it included only a narrow range of appellants, but it did include objecting members in a class suit.

During the same era in which the Court was developing the narrow right of quasi parties to appeal in limited circumstances, it was also considering numerous cases involving the "well settled maxim of the law, that 'no person can bring a writ of error to reverse a judgment who is not a party or privy to the record.'" *Bayard* v. *Lombard*, 50 U.S. (9 How.) 529, 551 (1850).[6] Rather than calling into question

[5] See, *e.g.*, F. Calvert, *A Treatise Upon The Law Respecting Parties To Suits In Equity* 55-66 (1847). See also *Minnesota Co.*, 69 U.S. (2 Wall.) at 634 n.† (citing Calvert's treatise); *Blossom*, 68 U.S. (1 Wall.) at 656 n.1 (same).

[6] See, *e.g.*, *Litchfield* v. *Goodnow*, 123 U.S. 549, 551-552 (1887) (holding that administrator of lands distinct from those at issue in underlying suit was "in law a stranger to the proceedings, and in no way bound thereby," and thus was not a party or in privity to afford a right of appeal); *Indiana S. R.R.* v. *Liverpool, London & Globe Ins. Co.*, 109 U.S. 168, 173 (1883) (where leave to join suit as a party is denied, person cannot appeal from final decree); *Ex parte Cockcroft*, 104 U.S. 578, 579 (1881)

the general principle that only a party or a privy to the record may appeal, the doctrine of quasi parties complemented—indeed exemplified—that rule. In more recent years, the Court has invoked the general principle that only parties may appeal without mentioning (and, presumably, without intending to cast doubt on) its quasi party cases. See, *e.g.*, *Marino* v. *Ortiz*, 484 U.S. 301, 304 (1988) (per curiam).

3. In the shareholder context, *Cohen* and similar cases suggest that adoption of the Federal Rules of Civil Procedure was not intended to affect adversely the rights of objecting shareholders as quasi parties to appeal approval of a settlement of a derivative action over their objections. As the owners of the corporation for whose benefit the derivative action is brought, shareholders are not strangers to the action.[7] Indeed, the relationship of the shareholder to the court's decision to approve a settlement is characteristic of a quasi party, as that phrase was used in this Court's cases.

When a particular shareholder brings a derivative action on behalf of the corporation, that shareholder becomes the

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(creditor heard in district court as a matter of favor not permitted to appeal where he was not a party and never asked to be one); *Ex parte Cutting*, 94 U.S. 14, 21-22 (1876) (stockholders could not appeal as parties where they had been denied leave to intervene and where the appeal sought a discretionary writ of mandamus); *Stacy* v. *Thrasher*, 47 U.S. (6 How.) 44, 49-50 (1848) (person not in privity can neither be bound by judgment nor appeal from it); *Ford* v. *Douglas*, 46 U.S. (5 How.) 143, 160 (1847) (same).

[7] In taking a contrary view, the court below opined that, since a derivative action is actually an action brought on behalf of the corporation, the decision to compromise the corporation's claim is not the shareholders', who "have no more right to speak for the firm or control its litigation decisions than bondholders or banks or landlords, all of whom have contractual interests that may be affected by litigation." Pet. App. 3a. The court also likened a corporation's shareholders to its "employees, vendors, and lawyers." *Ibid.*

representative of the corporation and all its shareholders in vindicating the rights of the corporation. *Hawes* v. *Oakland*, 104 U.S. 450, 460 (1881). See also *Cohen* v. *Beneficial Indus. Loan Corp.*, 337 U.S. 541, 548 (1949). Although the named plaintiff in a derivative action sues on behalf of the corporation, the shareholders necessarily benefit from whatever recovery the corporation may realize on its claims by the resulting enhancement of the value of their property. See 5 *Moore's Federal Practice* § 23.1.02[3][b] (D. Coquillette et al., eds., 3d ed. 1997) ("As an owner of securities in the corporation, the suing shareholder, along with all other shareholders, is harmed by an injury to the corporation.").

That principle is reflected in three provisions in Federal Rule of Civil Procedure 23.1. First, Rule 23.1(1) contains a "contemporaneous ownership" requirement that only a person who was a shareholder when the injury occurred may bring a derivative action. That requirement ensures that only a shareholder who has suffered an injury (by reason of stock ownership at the time the alleged injury occurred) may press the claim,[8] and establishes a necessary pre-condition that the derivative plaintiff's interests are aligned with those of the shareholders generally. See 5 *Moore's Federal Practice*, *supra*, at § 23.1.02[3][b]. Ownership of the corporation's stock, therefore, gives both the objecting shareholder and the plaintiff shareholder a shared interest in the outcome of the case.

Second, Rule 23.1 provides that a "derivative action may not be maintained if it appears that the plaintiff does not fairly and adequately represent the interests of the shareholders * * * similarly situated in enforcing the right of the corporation." That provision recognizes that the named plaintiff in a derivative action may only assert the

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[8] See, *e.g.*, *Daily Income Fund, Inc.* v. *Fox*, 464 U.S. 523, 531 n.6 (1984); 7C C. Wright et al., 7C *Federal Practice & Procedure: Civil* § 1828 at 60 (2d ed. 1986).

corporation's claim for the sole benefit of the shareholders, the owners of the corporation. See *Cohen* v. *Beneficial Indus. Loan Corp.*, 337 U.S. at 549 (A stockholder sues in a derivative action, "not for himself alone, but as representative of a class comprising all who are similarly situated.").

Most critically, Rule 23.1 provides that a shareholder derivative action "shall not be dismissed or compromised without the approval of the court, and notice of the proposed dismissal or compromise shall be given to shareholders or members in such manner as the court directs." The requirements are complementary. By ensuring that notice is given to all shareholders before a proposed dismissal or compromise settlement is entered by the court, Rule 23.1 sets in motion a process by which all shareholders must either formally participate in the proceedings or be bound by the decree without having given the court the benefit of their views on whether the court should enter the settlement.

The Rule requires fair notice to shareholders so that they may object in court to the proposed settlement. See, *e.g.*, *Maher* v. *Zapata Corp.*, 714 F.2d 436, 451 (5th Cir. 1983). By longstanding practice, objecting shareholders "must be allowed to have meaningful participation at a settlement hearing," including "certain rights to discovery and cross-examination on issues pertaining to the settlement." 5 *Moore's Federal Practice*, *supra*, at § 23.1.10[1][c]. The requirements of notice and an opportunity to object arise from the recognition that individual shareholders have a personal stake in the presentation of the claim on the corporation's behalf, and that settlement of the case will foreclose both the corporation and its shareholders from later pursuing the corporate claim, since entry of a settlement decree will have a preclusive effect on both the corporation and the shareholders with respect to that claim. See, *e.g.*, *Matsushita Elec. Indus. Co.* v. *Epstein*, 516 U.S. 367, 379 (1996).[9] The settlement hearing constitutes the only opportunity for a corporation's owners to exercise any measure of control over a corporate claim that, by definition, is not directed by the corporation's shareholder-elected managers. Rule 23.1 accordingly prevents a corporation's claim from being compromised without an opportunity for the corporation's owners to participate in the decision. Thus, because their underlying claim is the same as the named plaintiff-shareholders, notice is directed to them to show cause why the settlement should not be approved, under pain of losing their right to object at all yet being bound by the judgment. Once the Rule 23.1 notice is given, the judgment of the court approving the settlement has claim-preclusive effect on the objecting shareholders. In light of the foregoing specific factors, objecting shareholders may properly be regarded as quasi parties to the district court proceedings.

4. Although this Court's decisions recognize the rights of quasi parties to appeal, in only limited circumstances may a person who is not formally a named party to a case be regarded as a quasi party. In our view, in light of the

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[9] Notice also protects against due process concerns. See, *e.g.*, *Jones* v. *Nuclear Pharmacy, Inc.*, 741 F.2d 322, 325 (10th Cir. 1984) (citing *Baldwin* v. *Hale*, 68 U.S. (1 Wall.) 223, 233 (1863)) ("Parties whose rights are to be affected are entitled to be heard; and in order that they may enjoy that right they must first be notified."); *Maher*, 714 F.2d at 451 (holding that the "essential purpose of the notice [under Rule 23.1], with regard to the shareholders' due process rights, * * * [is to] fairly apprise the prospective members of the class of the terms of the proposed settlement and of the options that are open to them"). Cf. *Phillips Petroleum Co.* v. *Shutts*, 472 U.S. 797, 811-812 (1985) (holding that to bind an absent plaintiff in class action, State must provide "minimal procedural due process protection" including "notice plus an opportunity to be heard and participate in the litigation"); *Eisen* v. *Carlisle & Jacquelin*, 417 U.S. 156, 173 (1974) (notice to class members under Rule 23 "is designed to fulfill requirements of due process to which the class action procedure is of course subject").

importance of the regularity and certainty provided by the Federal Rules of Civil and Appellate Procedure and the potential for uncertain application of this Court's quasi party cases in other contexts, recognition of quasi party status in situations not covered in the federal rules of procedure should be sparing indeed.[10] Nonetheless, the Court's quasi party precedents do furnish significant support for the right of appeal in the objecting shareholder settlement context, because: Rule 23.1 specifically recognizes the shareholder's personal rights; this Court's cases arising prior to adoption of the Federal Rules of Civil Procedure involved similar types of interests, objections, and proceedings; and, until the decision below, the consistent practice since the adoption of the Federal Rules of Civil Procedure has been that objecting shareholders in a derivative action need not intervene before appealing the district court's decision to overrule their objections to the settlement.

Furthermore, persons recognized as being quasi parties for a particular purpose (here, objecting to a settlement) do not have unlimited rights of participation and appeal without formal intervention. First, under this Court's quasi party cases generally, the subject of the appeal may encompass only that aspect of the ancillary litigation over which the quasi party had a specific and recognized interest and as to which he actually participated in the district court. Thus, in *Kneeland* v. *American Loan & Trust Co.*, 136 U.S. 89, 94 (1890), the Court limited the scope of the "right of appeal * * * to all matters adjudicated after [the quasi party's] bid which affect the terms of that bid, or the burdens which he assumes thereby, and which are not withdrawn from his challenge by the terms of the decree under which he

[10] In a class action, for example, a question may arise whether an objector has standing as a class member to participate in the process. The parties presumably would have an opportunity to test that standing, just as they do when a motion to intervene is filed.

purchases." See also *Sage* v. *Railroad Co.*, 96 U.S. 712, 714 (1877); J. Story, *supra*, at 353. In the Rule 23.1 context, an objecting shareholder would have the right to appeal the district court's judgment only to the extent it overruled the objections and entered the settlement decree as a result. An objecting shareholder wishing to participate more expansively in the litigation would have to intervene formally as a party.

Second, the quasi party must have been the subject of an order or directed notice to appear in the district court proceedings and must have asserted a personal right that was merged into the court's ruling. See, *e.g.*, *Blossom*, 68 U.S. (1 Wall.) at 656. That assertion need not involve a formal intervention motion,[11] but it must be personal to the quasi party and be grounded in a cognizable legal interest.[12] Here, the objecting shareholder has a personal stake in the

[11] It is clear from this Court's cases concerning participation by persons deemed to be quasi parties that the Court often used the term "intervene" in the sense of participation in the district court proceedings, and not formal intervention through the filing of a complaint. See, *e.g.*, *Davis* v. *Mercantile Trust Co.*, 152 U.S. 590, 593 (1894) (describing how quasi party "was not a party to the record, either plaintiff or defendant; was never substituted for either; filed no bill, cross-bill, or answer; but was simply permitted to intervene, with liberty to be heard upon any and all proceedings for the protection of his interests as bondholder and stockholder"); *Williams* v. *Morgan*, 111 U.S. at 698-699 (describing how quasi parties "incidentally interested in some branch of a cause have been allowed to intervene for the purpose of protecting their interest"); *Trustees* v. *Greenough*, 105 U.S. 527, 536 (1881) (describing how, in the "vast amount of litigation which has arisen in this country upon railroad mortgages, where various parties have intervened for the protection of their rights, * * * it has been the common practice * * * to make fair and just allowances for expenses and counsel fees to the trustees" and to allow quasi parties to object to such awards).

[12] Thus, for example, a party's attorney sanctioned by a district court is a quasi party entitled to appeal that order without formal intervention, see, *e.g.*, *Collier* v. *Marshall, Dennehey, Warner, Coleman & Goggin*, 977 F.2d 93, 94-95 (3d Cir. 1992), cert. denied, 510 U.S. 977 (1993).

outcome of a derivative action settlement, is notified to show cause why the settlement should not be approved, and is entitled by law to object to settlement. He therefore may appeal without intervening. By contrast, a citizen who objects to entry of a government-sponsored settlement decree may not.[13] And a quasi party may not appeal an order

[13] See, *e.g.*, Antitrust Penalties and Procedure Act, 15 U.S.C. 16(b)-(h) (Tunney Act). Tunney Act proceedings afford an opportunity to the public to comment on settlements, and differ significantly from shareholder derivative suits. First, derivative suits are prosecuted on behalf of the corporation by a shareholder who otherwise stands on equal footing with all other shareholders, whereas the antitrust laws give the United States special status as champion of the public interest. Compare 15 U.S.C. 4, 25 (duty of government to institute proceedings to restrain antitrust violations) with 15 U.S.C. 15 (damage suits by persons injured in their business or property by antitrust violations), 26 (injunctive relief for persons threatened with loss or damage from antitrust violations). Moreover, a court's review of the Attorney General's exercise of discretion in reaching a settlement in such a case is necessarily deferential, in part to avoid constitutional questions that might otherwise arise. *Massachusetts School of Law at Andover, Inc.* v. *United States*, 118 F.3d 776, 783 (D.C. Cir. 1997). And unlike absent shareholders in derivative actions, those who are not formal parties to a government antitrust decree are not bound by it. See *id.* at 781; *United States v. LTV Corp.*, 746 F.2d 51, 53-54 & nn.5 & 6 (D.C. Cir. 1984) (per curiam) (concept of "privy to the record" includes absent shareholders in a derivative action who are bound by judgment; distinguishing non-parties in Tunney Act proceedings). Finally, non-parties who participate in Tunney Act proceedings without intervening do so pursuant to specific statutory authorization providing for such participation. See 15 U.S.C. 16(f)(3). Intervention would be required as a prerequsite to a Tunney Act appeal. See, *e.g.*, *LTV Corp.*, 746 F.2d at 54 ("those who object to the entry of a consent judgment must seek to intervene in the proceedings * * * as a condition of taking an appeal").

Like the antitrust enforcement settlement process, many environmental suits involving the government represent the public interest at large (as opposed to a corporation's financial interest), and thus courts afford deference to settlements reached between the government and a private party. Such cases routinely provide notice and an opportunity for public comment to the government before entry of a settlement by a court,

that does not have a binding effect on its actions or otherwise is not a final order. See, *e.g.*, *Webster Coal & Coke Co.* v. *Cassatt*, 207 U.S. 181, 187 (1907) (noting that "[t]here was here no attachment for contempt, no judgment on default, and no independent and collateral proceeding, the order disposing of which could be considered as a final decree").

B. Upholding The Rights Of Objecting Shareholders To Appeal District Court Decisions Approving Settlements Furthers The Purposes Underlying Rule 23.1

Rule 23.1 protects absent shareholders from settlements that unfairly compromise their interests by providing them with notice of and an opportunity to object to settlements and by requiring court approval of settlements. Affording objecting shareholders the narrow right to appeal the overruling of their objections furthers that important purpose.

1. Prior to the adoption of Rule 23 in 1938 (in which the notice and court-approval requirements were first provided),

but would not afford persons who comment quasi party status. See, *e.g.*, Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA), 42 U.S.C. 9622(d)(2); Solid Waste Disposal Act (SWDA), 42 U.S.C. 6973(d); see also 28 C.F.R. 50.7 (Department of Justice policy providing for public notice and comment on settlements of environmental claims seeking to abate the discharge of pollutants). Those situations are quite different from the derivative suit settlement at issue here. In environmental settlements, members of the general public are given an opportunity to make their views known but are not the subjects of a show cause order or a directed notice and thus are not given a direct right to participate as litigants without first intervening to become a party; the general rule is that one must intervene in order to litigate (including appeal). Indeed, the federal statutes involved generally contain provisions concerning intervention. See CERCLA, 42 U.S.C. 9613(i); SWDA, 42 U.S.C. 6972(b)(1) & 6972(b)(2)(E); see also 28 C.F.R. 50.7 (DOJ policy reserves right to oppose intervention).

some courts allowed the named stockholder unilaterally to dismiss or compromise the derivative action without notifying the other stockholders and without approval of the court. See C. McLaughlin, *Capacity of Plaintiff-Stockholder to Terminate a Stockholder's Suit*, 46 Yale L.J. 421, 430-432 (1937).[14] Equity Rule 27 then in effect did not require notice to stockholders or court approval in the event of a dismissal or compromise. McLaughlin recommended that to protect the absent stockholders, the court should be required to approve the settlement. *Id.* at 433-35.

The 1938 drafters of Rule 23 agreed with McLaughlin, citing his article in support of the new requirement of notice to absent shareholders and court approval of any proposed dismissal or compromise of a stockholder derivative action. See Rule 23 Advisory Committee Notes, note to subdivision (c) (1937). As Professor Moore stated in explaining the purpose of Rule 23(c), "notice will tend to lessen strike suits by shareholders, since a shareholder and his counsel will not be able to sue and settle in the dark; and it will prevent unrighteous compromise of a just shareholders' action." J. Moore & M. Cohn, *Federal Class Actions–Jurisdiction and Effect of Judgment*, 32 Ill. L. Rev. 555, 556 (1938). The 1966 amendments to Rule 23, which separated out derivative actions for treatment in a new Rule 23.1, did not make any change to the notice and approval process in shareholder derivative actions.

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[14] As McLaughlin explained, "[t]o allow a single stockholder or group of stockholders the power to make a private compromise of the corporate cause of action places a heavy reliance upon their judgment," which raises the problem that the corporation's claim is "at the mercy of individuals who have no hope of personal recovery even if the suit is prosecuted successfully, and who stand to suffer considerable losses in costs if unsuccessful; obviously a wide door is opened to strike suits and collusive payments to stockholders which may rarely, if ever, be recovered by the corporation." 46 Yale L.J. at 430.

Rule 23.1 thus embodies the historical recognition that, although plaintiffs and their counsel ordinarily strive to act conscientiously in the best interests of the shareholders, self-designated shareholder plaintiffs and their counsel do not invariably further those interests. A derivative plaintiff may misapprehend the strength of the case or the value of the settlement; plaintiffs' counsel may lack the strength of will to see a case to conclusion; and in rare instances a settlement may even involve faithlessness, dishonesty, or collusion among the parties. "There can be no blinking at the fact that the interests of the plaintiff in a stockholder's derivative suit and of his attorney are by no means congruent." *Saylor* v. *Lindsley*, 456 F.2d 896, 900 (2d Cir. 1972) (Friendly, J.). See also *Bell Atlantic Corp.*, 2 F.3d at 1309 ("Courts and commentators have long recognized the 'agency costs' inherent in class and derivative actions where the client, as principal, is neither well-situated nor adequately motivated to closely monitor and control the attorney, his agent.") (footnotes omitted).

2. Notice directed to shareholders informs them of a proposed settlement so that they may assess its adequacy and affords them an opportunity to object to a settlement that does not protect their interest.[15] The requirement of

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[15] The notice informs shareholders of the substantive terms of the proposed settlement and orders them to show cause why the settlement should not be approved as fair, reasonable and adequate to the corporation. The notice specifies that shareholders may object (usually in writing), informs them of the time and place for a hearing on whether the settlement should be approved, and warns the shareholders that approval of the settlement will bar all future claims. See, *e.g.*, *Maher* v. *Zapata Corp.*, 714 F.2d 436, 450-453 (5th Cir. 1983); *White* v. *Auerbach*, 500 F.2d 822, 823 (2d Cir. 1974); *Greenspun v. Bogan*, 492 F.2d 375, 378 (1st Cir. 1974); *Bernstein* v. *Mediobanca Banca di Credito Finanzario-Societa Per Azioni*, 78 F.R.D. 1, 3 (S.D.N.Y. 1978); *Boggess* v. *Hogan*, 410 F. Supp. 433, 442-443 (N.D. Ill. 1975); *In re National Student Marketing Litig.*, 68 F.R.D. 151, 152 (D.D.C. 1974); *Glicken* v. *Bradford*, 35 F.R.D. 144, 148 (S.D.N.Y. 1964). See also *Manual for Complex Litigation 3d* §§ 30.41,

court approval of any settlement is intended to protect further the interests of absent shareholders. "It is well established that a court should not merely rubber stamp whatever settlement is proposed by the parties to a shareholder derivative action. A court must, instead, exercise judgment sufficiently independent and objective to safeguard the interests of shareholders not directly involved in the action." *Greenspun* v. *Bogan*, 492 F.2d 375, 378 (1st Cir. 1974). Cf. *In re Jiffy Lube Securities Litig.*, 927 F.2d 155, 158 (4th Cir. 1991) ("The primary concern addressed by Rule 23(e) is the protection of class members whose rights may not have been given adequate consideration during the settlement negotiations."). The court may not approve a settlement without finding it to be "fair, reasonable and adequate." *Jones* v. *Nuclear Pharmacy, Inc.*, 741 F.2d 322, 324 (10th Cir. 1984); see also *Granada Investments, Inc.* v. *DWG Corp.*, 962 F.2d 1203, 1205 (6th Cir. 1992).[16]

The objecting shareholders play a pivotal role in the settlement approval process, since they alone have the incentive to attempt to stop a process that builds momentum from the moment a deal is struck between the derivative

33.36 ("Objections may be raised not only by class members but also by parties seeking to intervene under Fed. R. Civ. P. 24."). The order in this case conformed to those general types, providing that "[a]ny shareholder of record of ADM as of May 29, 1997, may appear and show cause * * * why the proposed settlement of the derivative claims embodied in the Stipulation should or should not be approved as fair, reasonable and adequate." Order, No. 95-CV-2279 (C.D. Ill. May 30, 1997).

[16] The Seventh Circuit's statement that the only purpose of notice under Rule 23.1 is so "that other investors may contest the faithfulness or honesty of the self-appointed plaintiff" is belied by the established focus of a district court's inquiry in determining whether the substantive terms of settlement are fair to shareholders and the corporation. The proper scope of the inquiry at the settlement hearing also is demonstrated by what is set forth in the notice under Rule 23.1, which does not restrict objectors to contesting the good faith of the representative. See *supra* note 15.

plaintiff and the defendant.[17] Once the derivative plaintiff and the defendant have come to terms, they are advocates for their settlement, a development that deprives the court of the benefit of an adversarial presentation on the question Rule 23.1 directs the court to decide: whether the settlement is in the best interests of all shareholders, named and absent alike. When the once-adversaries, now prospective settling parties, present an agreement to the court, "[a]ll the dynamics conduce to judicial approval of such settlements." *Alleghany Corp.* v. *Kirby*, 333 F.2d 327, 347 (2d Cir. 1964) (Friendly, J., dissenting), aff'd en banc by equally divided court, 340 F.2d 311 (2d Cir. 1965), cert. dismissed, 384 U.S. 28 (1966). Objecting shareholders, therefore, serve a critical function because they alone have the incentive to inform the court that a proposed settlement is deficient, disadvantageous, or unfair to all shareholders.[18]

3. The opportunity to challenge settlements of those private disputes in the district court without the corresponding right to appeal is not sufficient when there is a natural tendency among trial courts to favor approving settlements to which the named parties have agreed. In that sense, "[j]udicial approval of the settlement is an imperfect safeguard." J. Coffee, Jr., *The Unfaithful Champion: The Plaintiff as Monitor in Shareholder Litigation*, Law & Contemp. Probs., Summer 1985, 5, 31.

[17] By contrast, such concerns are significantly less pronounced under statutory regimes that provide for settlement of actions brought by the government to enforce various laws because of the broader public interest the government is entrusted to protect. See *supra* note 13.

[18] See *Bell Atlantic Corp.*, 2 F.3d at 1310 (objectors give court access to information on the settlement's merits); *Papilsky* v. *Berndt*, 466 F.2d 251, 258 (2d Cir. 1972) (notice is essential to ensure resolution in best interest of corporation and absent shareholders); *Cohen*, 127 F.2d at 724-725 (court benefits from broader view of the settlement provided by objectors).

An unfettered, though narrowly tailored, right to appeal the district court's decision to approve the settlement will further the purposes underlying Rule 23.1 by ensuring the opportunity for appellate scrutiny of what otherwise would be largely unreviewable proceedings. In that sense, normal intervention may not be a viable alternative for the shareholder whose objections are overruled. The district court may be too readily disposed to find that an objecting shareholder was adequately represented within the meaning of Federal Rule of Civil Procedure 24, and thus deny intervention, if it also concludes that the settlement was fair, reasonable and adequate within the meaning of Rule 23.1. Moreover, the standards for objecting under Rule 23.1 are different from intervention under Rule 24, and it was precisely that point that the *Cohen* court recognized in ruling that an objecting shareholder had a limited right to appeal without demonstrating that the standards for intervention had been satisfied. See 127 F.2d at 724-725; see also *Bell Atlantic Corp.*, 2 F.3d at 1310 (cautioning against the erection of "obstacles to challenging derivative action settlement agreements").

C. The Court Of Appeals' Contrary Reasoning Is Unpersuasive

The court of appeals concluded that if the objecting shareholders wished to appeal, they must first intervene as parties. As a practical matter, that conclusion imposes an unnecessary requirement. By appealing the district court's approval of the settlement, the objecting shareholders are merely seeking to persuade the court of appeals that the district court erred in rejecting the arguments they were required to make if they hoped to avert the imposition of a binding judgment adverse to their interests. Requiring intervention as a party for the purpose of making an appearance in the court of appeals threatens to interpose an unwarranted obstacle to what historically has been an

essentially automatic right that comparably situated quasi parties have had to pursue their appeals.[19]

As a matter of law and precedent, the court of appeals' reliance on this Court's decision in *Marino* v. *Ortiz*, 484 U.S. 301 (1988), is misplaced. In *Marino*, a class action had been brought by groups representing minority police officers who challenged promotion practices by the New York City Police Department. The lawsuit was settled by consent decree. The decree was appealed, not by minority officers who were members of the class, but by a group of white officers, who had objected to the decree in district court but had not sought to intervene as parties in the case. This Court held that they could not appeal the consent decree without intervening. Observing that "[t]he rule that only parties to a lawsuit, or those that properly become parties, may appeal an adverse judgment," the Court explained that "because petitioners were not parties to the underlying lawsuit, and because they failed to intervene for purposes of appeal, they

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[19] We are particularly concerned about the Seventh Circuit's suggestion that absent shareholders must demonstrate that the named representative has been dishonest or unfaithful in order to intervene for purposes of appeal. If that view were correct, even if the shareholders were interested only in objecting to the fairness of a settlement, they nonetheless would have to meet the heavier burden of proving bad faith by the class representative before being permitted to appeal. The fairness of a settlement does not turn simply on the good faith of the representative. Other courts, moreover, have held that a represented party must intervene prior to the settlement process. See *Walker* v. *City of Mesquite*, 858 F.2d 1071, 1074 (5th Cir. 1988) (describing motion to intervene after entry of consent decree as "untimely"); *Guthrie* v. *Evans*, 815 F.2d 626, 628 (11th Cir. 1987) (class member may intervene as a matter of right "in the course of the class action" to monitor representation of his rights). We disagree with such a requirement because judicial administration is ill-served by requiring absent class members or shareholders to submit formal intervention motions simply to preserve their right to appeal a settlement that has yet to be proposed or accepted. See *American Pipe & Constr. Co.* v. *Utah*, 414 U.S. 538, 560-561 (1974).

may not appeal from the consent decree approving that lawsuit's settlement." *Marino*, 484 U.S. at 304.

Marino is distinguishable from this case. Although the interests of the white police officers were affected in some sense by the consent decree in *Marino*, the action did not involve any legal claim on their behalf; they were otherwise strangers to the lawsuit; and they were not precluded by the judgment from subsequently litigating any claims they might have. See *Martin* v. *Wilks*, 490 U.S. 755, 763 (1989). Thus, the non-party police officers in *Marino* were quite different from the quasi-party objecting shareholders in this case.[20] Here, the shareholders' personal interests in their corporation's claim have been asserted on the shareholders' behalf by the named plaintiff; the appealing shareholders have appeared in district court in response to a show cause notice to litigate the propriety of the settlement; and the appealing shareholders will be foreclosed by the judgment from pursuing those claims henceforth.[21]

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[20] Congress, of course, can limit challenges to a consent decree by individuals whose claims were not asserted in the original action but whose rights, nevertheless, are affected by the decree. For example, after *Martin* v. *Wilks*, in 1991 Congress amended Title VII, 42 U.S.C. 2000e et seq., to provide that any person who is given actual notice of a proposed decree and who might be affected by it must state his or her objections to the court reviewing the settlement at that time and may not file a later challenge to the decree. See 42 U.S.C. 2000e-2(n). Thus, in a situation like that presented in *Marino*, white officers with notice of a decree that might affect their rights would have to appear in that court to file their objections. Section 2000e-2(n) does not purport to change the rule in *Marino* that such a person must intervene in order to appeal. The preclusive effect of the judgment, however, may give substantial support to a motion to intervene.

[21] In neither *Marino* itself nor the sole decision cited on the issue, *United States ex rel. Louisiana* v. *Jack*, 244 U.S. 397 (1917), did the Court call into question the many prior cases in which it had upheld the rights of quasi parties to appeal. Rather, the Court simply invoked the long-standing general rule that only a party or a privy to the record may

The court of appeals also based its holding on Federal Rule of Appellate Procedure 3(c), which provides: "A notice of appeal must specify the *party or parties* taking the appeal by naming each appellant in either the caption or the body of the notice of appeal." See Pet. App. 2a (emphasis added by Seventh Circuit decision). That rule, however, addresses the contents of the notice and does not limit the "parties" on appeal to only those persons who were formally made "parties" in the district court proceedings. The court of appeals appears to have read "party or parties" to mean only those listed in the district court's caption. Such a reading conflicts with well-settled case law allowing appellants who were not parties below to be listed in the notice of appeal and to prosecute their appeal. See, *e.g.*, *United Airlines, Inc.* v. *McDonald*, 432 U.S. 385 (1977) (permitting non-party to appeal denial of a motion for leave to intervene); *Collier* v. *Marshall, Dennehey, Warner, Coleman & Goggin*, 977 F.2d 93, 94-95 (3d Cir. 1992) (attorney appealing order in which he is sanctioned must be listed in notice of appeal); *Mylett* v. *Jeane*, 879 F.2d 1272, 1275 (5th Cir. 1989) (per curiam) (same); *FTC* V. *Amy Travel Serv., Inc.*, 875 F.2d 564 (7th Cir. 1989) (same); *DeLuca* v. *Long Island Lighting Co.*, 862 F.2d 427, 429-430 (2d Cir. 1988) (same). See also *Miltier* v. *Downes*, 935 F.2d 660, 662-663 & n.1 (4th Cir. 1991) (same); *Aetna Life Ins. Co.* v. *Alla Medical Servs.*, 855 F.2d 1470, 1473 (9th Cir. 1988) (allowing counsel to appeal sanction order even though not a party below and not explicitly listed as a party to the appeal). See generally 15A C. Wright *et al.*, *Federal Practice and Procedure Jurisdiction* § 3902.1 (2d ed. 1992). Plainly, then, "the party or parties taking the appeal" cannot be limited to the named parties below. The far more natural reading of Federal Rule of Appellate Procedure 3(c)—consistent with its notice-serving function—is that a

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appeal. See *Marino*, 484 U.S. at 587; *Jack*, 244 U.S. at 402 (quoting *Bayard* v. *Lombard*, 50 U.S (9 How.) 530, 551 (1850)).

"notice of appeal must specify [who is] taking the appeal." And that reading offers no support for the Seventh Circuit's position.[22]

Finally, the court of appeals also based its decision on the conclusion that allowing shareholder objectors to appeal the settlement without intervention would "fragment the control" of the action. Pet. App. 4a. That reasoning disregards Rule 23.1's recognition that other shareholders are entitled to participate in the district court to object to a settlement proposed by the named-plaintiff shareholder. The Federal Rules plainly do not evince a concern that that limited degree of participation by persons other than the named plaintiff will unduly disrupt the litigation or render it unmanageable. In any event, an appeal by a quasi-party objecting shareholder would not raise those issues, since the appeal would be confined to the discrete legal issue whether the district court abused its discretion in approving the settlement. See *In re Pacific Enterprises Sec. Litig.*, 47 F.3d 373, 377 (9th Cir. 1995); *Bell Atlantic Corp.*, 2 F.3d at 1305-1306.[23]

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[22] On December 1, 1998, the new Federal Rules of Appellate Procedure will take effect. The new Rule 3(c) is similar to the old rule in that it does not specify that a "party" must be a named party in the district court. New Rule 3(c)(3), however, does contain a new provision for class actions, providing that "the notice of appeal is sufficient if it names one person qualified to bring the appeal as representative of the class."

[23] If, contrary to our submission, the Court were to conclude that the historical practice concerning quasi parties and the explicit confirmation of individual shareholder interests in Rule 23.1 are insufficient, absent intervention, to allow an objecting shareholder to take an appeal of a district court judgment approving a settlement, the Court should make clear that Rule 24 should be interpreted and applied in this special setting in a way that ensures that intervention will be routinely granted so as to effectuate fully the purposes of Rule 23.1 (and the quasi party cases) of facilitating objections in the district court in matters directly affecting shareholders' interests and appeal of district court judgments that reject those objections. See *Bryant* v. *Yellin*, 447 U.S. 352, 366 (1980) (concluding that intervention after judgment by affected residents was permissible for the purpose of taking appeal where government suing on behalf of public interest decided to forgo appeal). In the alternative, the Federal Rules of Civil and Appellate Procedure could be amended to address the problem.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1998

CALIFORNIA PUBLIC EMPLOYEES RETIREMENT SYSTEM AND FLORIDA STATE BOARD OF ADMINISTRATION,

Petitioners,

v.

PAUL FELZEN, ET AL.,

Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

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BRIEF OF PROFESSORS LAWRENCE A. HAMERMESH AND MARY BRIGID McMANAMON AS *AMICI CURIAE* SUPPORTING PETITIONERS

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32 pp

TABLE OF CONTENTS

TABLE OF AUTHORITIES ii

INTEREST OF THE *AMICI* 1

SUMMARY OF ARGUMENT 2

ARGUMENT 3

I. IN DERIVATIVE ACTIONS ASSERTING CLAIMS ARISING UNDER STATE LAW, STATE LAW RULES REGARDING THE CONDUCT OF DERIVATIVE ACTIONS AND THE PROSECUTION OF APPEALS IN SUCH ACTIONS SHOULD GOVERN DERIVATIVE ACTIONS IN THE FEDERAL COURTS. 3

II. THE COURT BELOW UNDERESTIMATED THE SIGNIFICANCE OF THE OBJECTORS' INTEREST IN THE DERIVATIVE ACTION AS A MATTER OF SUBSTANTIVE LAW. 15

III. UNSUCCESSFUL OBJECTORS IN THE DELAWARE COURTS MAY APPEAL SETTLEMENT APPROVALS IN DERIVATIVE ACTIONS WITHOUT FORMAL INTERVENTION. 21

CONCLUSION 25

TABLE OF AUTHORITIES

Cases

Bangor Punta Operations, Inc. v. Bangor & Aroostook R.R., 417 U.S. 703 (1974) 5
Bell Atl. Corp. v. Bolger, 2 F.3d 1304 (3d Cir. 1993) . 8
Braun v. Fleming-Hall Tobacco Co., Inc., 92 A.2d 302 (Del. 1952) 21, 22
Burghart v. Landau, 821 F. Supp. 173 (S.D.N.Y. 1993). 6
Byrd v. Blue Ridge Rural Electric Cooperative, Inc., 356 U.S. 525 (1958) 13, 14
Cohan v. Loucks, 1993 WL 121855 (Del. Ch. 1993) . 23
Cohen v. Beneficial Indus. Loan Corp., 337 U.S. 535 (1949) 5
Cohen v. Young, 127 F.2d 721 (6th Cir. 1942) . . . 7
Daily Income Fund, Inc. v. Fox, 464 U.S. 523 (1984) . 16
Erie Railroad v. Tompkins, 304 U.S. 64 (1938) . . . 3
Gallup v. Caldwell, 120 F.2d 90 (3d Cir. 1941) . . . 4
Gasperini v. Center for Humanities, Inc., 518 U.S. 415 (1996) 7
Geller v. Tabas, 462 A.2d 1078 (Del. 1983) 23
Girsh v. Jepson, 521 F.2d 153 (3d Cir. 1975) 7
Gladstone v. Bennett, 153 A.2d 577 (Del. 1959) . .23
Goodman v. Futrovsky, 213 A.2d 899 (Del. 1965) . . . 23
Greenspun v. Bogan, 492 F.2d 375 (1st Cir. 1974) . 7
Grimes v. Donald, 673 A.2d 1207 (Del. 1996) 16
Hanna v. Plumer, 380 U.S. 460 (1965) 14, 15

Hawes v. Oakland, 104 U.S. 450, 26 L. ed. 827 (1881) 3, 4
Heineman v. Datapoint Corp., 611 A.2d 950 (Del. 1992). 17, 18
HFG Co. v. Pioneer Publ'g Co., 162 F.2d 536 (7th Cir. 1947). 5
Hoffmann v. Dann, 205 A.2d 343 (Del. 1964) 23
In re Pittsburgh & Lake Erie R.R. Sec. & Antitrust Litig., 543 F.2d 1058 (3d Cir. 1976) 6
In re Resorts Int'l Shareholder Litigation Appeals, 570 A.2d 259 (Del. 1990). 24
In re Storage Tech. Corp. Sec. Litig., 804 F. Supp. 1368 (D. Colo. 1992). 6
Jones v. Nuclear Pharmacy, Inc., 741 F.2d 322 (10th Cir. 1984) 7
Kahn v. Sullivan, 594 A.2d 48 (Del. 1991). 24
Kamen v. Kemper Fin. Servs., Inc., 500 U.S. 90 (1991) 5
Kaplan v. Wyatt, 499 A.2d 1184 (Del. 1985). 18
Krinsky v. Helfand, 156 A.2d 90 (Del. 1959). 23
Levine v. Smith, 1987 Del. Ch. LEXIS 524 (Del. Ch. 1987), *aff'd*, 591 A.2d 194 (Del. 1991). 18, 19
Lewis v. Chiles, 719 F.2d 1044 (9th Cir. 1983) . . . 6
Lewis v. Fuqua Industries, Inc., 1982 WL 8783 (Del. Ch. 1982) 23
Lewis v. Hirsch, 1995 Del. LEXIS 62 (Del. Ch. 1995) . 20
Manacher v. Reynolds, 165 A.2d 741 (Del. Ch. 1960) 23
Marino v. Ortiz, 484 U.S. 301 (1988). 10
Masterson v. Pergament, 203 F.2d 315 (6th Cir. 1953) 7
Matsushita Elec. Indus. Ltd. v. Epstein, 516 U.S. 367 (1996) 25

Moses v. Pickens, 1982 WL 17825 (Del. Ch. 1982) . . 23
Nathan v. Rowan, 651 F.2d 1223 (6th Cir. 1981) . 10, 11
Neponsit Investment Co. v. Abramson, 405 A.2d 97 (Del. 1979) 23
Neuwirth v. Allen, 338 F.2d 2 (2d Cir. 1964) 7
Norton v. National Research Found., 141 F.R.D. 510 (D. Kan. 1992) 6
Osborn v. Bank of the United States, 22 U.S. (9 Wheat.) 738 (1824) 9, 10
Pianta v. H.M. Reich Co., 77 F.2d 888 (2d Cir. 1935) . 11
Pogostin v. Rice, 480 A.2d 619 (Del. 1984) 16
Polk v. Good, 506 A.2d 531 (Del. 1986) 23, 24
Prezant v. DeAngelis, 636 A.2d 915 (Del. 1994) . . . 24
Ragan v. Merchants Transfer & Warehouse Co., 337 U.S. 530 (1949) 12
Rales v. Blasband, 634 A.2d 927 (Del. 1993) 16
RCM Sec. Fund, Inc. v. Stanton, 928 F.2d 1318 (2d Cir. 1991) 6
Rome v. Archer, 197 A.2d 49 (Del. 1964) 23
Rosenbaum v. MacAllister, 32 F.3d 1439 (10th Cir. 1995) 8
Rutman v.Kaminsky, 226 A.2d 122 (Del. 1967) . . . 23
S.A. Healy Co. v. Milwaukee Metropolitan Sewerage Dist., 60 F.3d 305 (7th Cir. 1995) 12
Salve Regina College v. Russell, 499 U.S. 225 (1991) 7
Saminsky v. Abbott, 194 A.2d 549 (Del. Ch. 1963) . . 23
Shults v. Champion Int'l Corp., 35 F.3d 1056 (6th Cir. 1994) 8
Spiegel v. Buntrock, 571 A.2d 767 (Del. 1990) . . . 16

Stepak v. Ross, 1985 WL 21137 (Del. Ch. 1985) . . 23
Torres v. Oakland Scavenger Co., 487 U.S. 312 (1988) 14
Tryforos v. Spanos, 518 F.2d 1258 (7th Cir. 1975), cert. denied, 423 U.S. 1091 (1976) 8
United Founders Life Ins. Co. v. Consumers Nat'l Life Ins. Co., 447 F.2d 647 (7th Cir. 1971) 7
United States ex rel. Louisiana v. Jack, 244 U.S. 397 (1917) 11
Walker v. Armco Steel Corp., 446 U.S. 740 (1980) . . 12
Wolgin v. Simon, 722 F.2d 389 (8th Cir. 1983) . . . 6
Zapata Corp. v. Maldonado, 430 A.2d 779 (Del. 1981) 16

Constitution, Statutes and Rules

U.S. Const., Art. III 9
28 U.S.C. § 1253 9
28 U.S.C. § 1291 9
28 U.S.C. § 2072 . . . . . 12, 13
8 *Del. C.* §141(a) 16
Delaware Chancery Court Rule 23.1 19
Fed. R. App. P. 3(c) 11, 12
Fed. R. Civ. P. 3 12
Fed. R. Civ. P. 68 13
Fed. R. Civ. P. 23.1 8
Fed. R. Civ. P. 23.1 8
Fed. R. Civ. P. 23(b) 3, 5

Other Materials

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1947 Special Pamphlet to 28 U.S.C. §§ 721-723 . . 5
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BRIEF OF PROFESSORS LAWRENCE A. HAMERMESH AND MARY BRIGID McMANAMON AS *AMICI CURIAE* SUPPORTING PETITIONERS

The undersigned respectfully submit this brief as *amici curiae* supporting the petitioners, California Public Employees' Retirement System and Florida State Board of Administration.[1]

INTEREST OF THE *AMICI*

Professor Lawrence A. Hamermesh is Associate Professor of Law, Widener University School of Law, Wilmington, Delaware. A member of the Delaware Bar since 1976, Professor Hamermesh practiced law in Wilmington, Delaware, until 1994, principally in the field of corporate litigation, including stockholder derivative and class action litigation. Professor Hamermesh teaches courses in business organizations, securities regulation, corporate finance, and mergers and acquisitions. Professor Hamermesh's interest in submitting this *amicus* brief is in ensuring that the Court is duly apprised of the substantive law and practice of Delaware in relation to stockholder derivative actions.

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[1] No counsel for a party authored any part of this brief. The Council of Institutional Investors, which is an association of institutional investors, is making a monetary contribution to the preparation and submission of this brief. The parties consented to the filing of this brief, as reflected in letters on file with the Court.

Wilmington, Delaware. She has been teaching in the field of federal procedure, including courses in Civil Procedure, Federal Courts, Complex Litigation, and Conflict of Laws, since 1985. In addition, she has published law review articles on the history of federal procedure and has been a co-author of one of the major casebooks on Civil Procedure since 1997. Professor McManamon's interest in submitting this *amicus* brief is in ensuring that the Court is duly apprised of the historical practice under Federal Rule of Civil Procedure 23.1, with particular emphasis on the federalism concerns raised by the Seventh Circuit's creation of new federal common law.

SUMMARY OF ARGUMENT

1. In a stockholder derivative action, the law of the state of incorporation of the entity on behalf of which claims are being asserted should determine the entitlement of a stockholder to appeal approval of a settlement of the action, just as the law of the state of incorporation determines the entitlement of a stockholder to initiate and conduct the action.

2. In declining to permit a stockholder to appeal approval of a settlement without formally intervening as a party, the court below underestimated the stockholder's interest in such a settlement as a matter of applicable state substantive law, here Delaware law.

3. Consistent with the interest of stockholders as a matter of substantive law in the settlement of a derivative action on behalf of a Delaware corporation,

the Delaware courts have consistently allowed objectors to a settlement of such an action to appeal approval of a settlement without having formally intervened as a party. This Court should direct that this approach be followed in this case.

ARGUMENT

I. IN DERIVATIVE ACTIONS ASSERTING CLAIMS ARISING UNDER STATE LAW, STATE LAW RULES REGARDING THE CONDUCT OF DERIVATIVE ACTIONS AND THE PROSECUTION OF APPEALS IN SUCH ACTIONS SHOULD GOVERN DERIVATIVE ACTIONS IN THE FEDERAL COURTS.

In 1938, this Court both promulgated Federal Rule of Civil Procedure 23(b), now Rule 23.1, and limited its scope by holding in *Erie Railroad v. Tompkins*, 304 U.S. 64, 78 (1938), that, "[e]xcept in matters governed by the Federal Constitution or by acts of Congress, the law to be applied in any case is the law of the state." The impact of this holding on former Rule 23(b) was recognized immediately. At the Proceedings of the Institute on Federal Rules held July 21, 1938, William D. Mitchell, chair of the Supreme Court Advisory Committee, noted:

> Many years ago, in *Hawes v. Oakland*, 104 U.S. 450, 26 L. ed. 827 (1881), the Supreme Court held, as an equitable principle, that a shareholder could not maintain [a derivative action on behalf of the corporation] if he did not own

the shares when the act complained of was committed.

. . . .

Now, if the question of the right to maintain suit, depending on whether the plaintiff owned the shares when the act was complained of or not, is a matter of substantive right, then it is possible under *Erie Railroad v. Tompkins*, which now makes the decision of the state court binding on federal courts in the matter of substantive law, that the court may say that this question of the right of a shareholder to sue and the condition on which his right is predicated, is a matter of state law, and the federal courts no longer may have a rule of their own, but must follow the local state decisions on that point.

Proceedings of the American Bar Association Institute on Federal Rules at Cleveland, Ohio 184 (W. Dawson ed. 1938).

Mr. Mitchell's concern proved well-founded, as the federal courts immediately had to grapple with the question of whether Rule 23(b) impermissibly affected substantive rights. As early as 1941, the Third Circuit held that a shareholder's ability to participate in the litigation of a derivative suit is a substantive issue, which must be determined in a diversity action by the law of the state of incorporation. *Gallup v. Caldwell*, 120 F.2d 90, 93 (3d Cir. 1941). After some early confusion on this

issue among the circuits,[2] this Court directed that Rule 23(b), and later Rule 23.1, should be interpreted so as not to affect substantive rights,[3] and the *Gallup* court's

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[2] In 1944, the Advisory Committee on Rules for Civil Procedure considered amending Rule 23(b), noting:

> As a result of the decision in Erie R. Co. v. Tompkins, 304 U.S. 64, 58 S.Ct. 817 (82 L.Ed. 1188, 114 A.L.R. 1487) (decided April 25, 1938, after this rule was promulgated by the Supreme Court, though before it took effect) a question has arisen as to whether the provision above quoted deals with a matter of substantive right or is a matter of procedure.

1947 Special Pamphlet to 28 U.S.C. §§ 721-723, at 19, *quoted in HFG Co. v. Pioneer Publ'g Co.*, 162 F.2d 536, 539 (7th Cir. 1947). The committee decided to do nothing at that time, however, concluding that "[t]here is reason to say that the question is one which should not be decided by the Supreme Court ex parte, but left to await a judicial decision in a litigated case." *Id.* at 22, *quoted in HFG Co.*, 162 F.2d at 539.

[3] *See, e.g.*, *Kamen v. Kemper Fin. Servs., Inc.*, 500 U.S. 90 (1991); *Cohen v. Beneficial Indus. Loan Corp.*, 337 U.S. 535 (1949); *see also Bangor Punta Operations, Inc. v. Bangor & Aroostook R.R.*, 417 U.S. 703, 713-14 (1974) (applying law of state of incorporation to question of standing in state law claims). In *Kamen*, this Court went so far as to hold that

position is now the generally accepted rule.[4] This rule, that the applicable substantive law governs a shareholder's right to participate in the litigation of a derivative suit, applies not only to the plaintiff, but also to a shareholder objecting to a proposed settlement. *See In re Pittsburgh & Lake Erie R.R. Sec. & Antitrust Litig.*, 543 F.2d 1058, 1065-67 (3d Cir. 1976) (holding standing to object to settlement of federal claim is federal law question). Given the very real problem of collusion in the settlement of shareholder derivative suits (*see* Br. of Amicus Curiae Council of Inst'l Investors Part I, A), the underlying substantive law recognizes that the objecting shareholder is every bit as important to the vindication of the corporation's rights as the named plaintiff. *See* discussion *infra* Part II.

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in a derivative action arising under *federal* law, the need for uniformity in corporate governance overcame any need for uniformity of federal practice, and thus a shareholder's standing should be determined by the law of the corporation's state of incorporation, unless that law frustrated federal objectives. 500 U.S. at 97-98.

[4] *E.g.*, *RCM Sec. Fund, Inc. v. Stanton*, 928 F.2d 1318, 1329-30 (2d Cir. 1991); *Wolgin v. Simon*, 722 F.2d 389, 391-92 (8th Cir. 1983); *Burghart v. Landau*, 821 F. Supp. 173, 176-78 (S.D.N.Y. 1993); *Norton v. National Research Found.*, 141 F.R.D. 510, 512 (D. Kan. 1992); *In re Storage Tech. Corp. Sec. Litig.*, 804 F. Supp. 1368, 1375 (D. Colo. 1992); *see Lewis v. Chiles*, 719 F.2d 1044, 1047-48 (9th Cir. 1983); *see also* 7C Charles Alan Wright *et al.*, *Federal Practice and Procedure* § 1826 (2d ed. 1986).

The objecting shareholder's role does not end with the approval of a settlement. The governing substantive law recognizes the importance of the objector's right to appeal such approval to assure vindication of the corporation's rights. *See* discussion *infra* Part III. It is entirely appropriate for the circuit courts, hearing appeals in diversity cases, to be sensitive to that important state interest. This Court has recently reminded us that that the principles of *Erie* govern the appellate courts, as well as the trial courts. *See Gasperini v. Center for Humanities, Inc*, 518 U.S. 415 (1996); *Salve Regina College v. Russell*, 499 U.S. 225 (1991). And the federal courts have recognized and been sensitive to the importance of the objecting shareholder in the derivative suit. In 1942, the Sixth Circuit expressly allowed such a shareholder to appeal the approval of a settlement without the need to intervene below. *Cohen v. Young*, 127 F.2d 721, 724 (6th Cir. 1942). Thereafter, the circuits routinely allowed objectors in shareholder derivative suits to appeal without intervening.[5] The Seventh Circuit itself declared:

> The law is clear that a non-party shareholder who appears, pursuant to a

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[5] *See, e.g.*, *Jones v. Nuclear Pharmacy, Inc.*, 741 F.2d 322 (10th Cir. 1984); *Girsh v. Jepson*, 521 F.2d 153 (3d Cir. 1975); *Greenspun v. Bogan*, 492 F.2d 375 (1st Cir. 1974); *United Founders Life Ins. Co. v. Consumers Nat'l Life Ins. Co.*, 447 F.2d 647 (7th Cir. 1971); *Neuwirth v. Allen*, 338 F.2d 2 (2d Cir. 1964); *Masterson v. Pergament*, 203 F.2d 315 (6th Cir. 1953).

> Rule 23.1 notice, to present objections to a proposed dismissal or settlement of a derivative action may appeal an adverse decision even though he has not been formally made a party to the action.

Tryforos v. Spanos, 518 F.2d 1258, 1263 n.22; *see* 3B James W. Moore, *Federal Practice* ¶ 23.1.24[3] (2d ed. 1996).

With the exception of the Seventh Circuit's opinion in the case at bar, no circuit has reversed its position on an objecting shareholder's right to appeal. Quite the contrary. Every circuit that has discussed the question in recent years has reaffirmed the objector's right to appeal without intervention. *See Rosenbaum v. MacAllister*, 32 F.3d 1439, 1441-43 (10th Cir. 1995) (allowing objector to appeal without intervention, noting difference between Rule 23 case and Rule 23.1 case); *Shults v. Champion Int'l Corp.*, 35 F.3d 1056, 1059-60 (6th Cir. 1994) (expressly reaffirming its earlier opinion in *Cohen v. Young*); *Bell Atl. Corp. v. Bolger*, 2 F.3d 1304, 1307-10 (3d Cir. 1993) (expressly holding that objecting shareholder may appeal without intervening).

In contrast, the Seventh Circuit, overruling precedent and showing no sensitivity to the very real regulatory concerns of the underlying state law, held that an objecting shareholder must intervene in order to appeal the approval of a settlement in a Rule 23.1 derivative action. Moreover, the court rejected the thoughtful reasoning of its own precedent as well as that of the other circuits and ignored the role that an objector plays in a derivative suit. Instead, the court below held

that it could not entertain the objector's appeal because it was outside the court's jurisdiction. The court's reasoning, however, cannot withstand close scrutiny.

When determining if a matter is within the jurisdiction of a federal court, the first place to look is the jurisdictional statute. In this case, the controlling statute is 28 U.S.C. § 1291. That section provides: "The courts of appeals . . . shall have jurisdiction of appeals from all final decisions of the district courts of the United States, . . . except where a direct review may be had in the Supreme Court." The Seventh Circuit had before it a final decision of the U.S. District Court for the Central District of Illinois, and this case is not one in which there may be a direct review in this Court, *cf. id.* § 1253 (providing for direct review from decisions of three-judge courts). Thus, there is no statutory bar to the Seventh Circuit's hearing this appeal.

This statutory grant of jurisdiction must, of course, be tested by the bounds of Article III of the U.S. Constitution. In this regard, there are two issues that must be addressed. First, is this case within the judicial power of the United States? As Chief Justice John Marshall declared, with the exception of those cases within the original jurisdiction of this Court, "the [judicial] power [of the United States] is to be exercised in its original or appellate form, or both, as the wisdom of Congress may direct." *Osborn v. Bank of the United States*, 22 U.S. (9 Wheat.) 738, 820 (1824). Thus, if this case is within the bounds of Article III in its original form, it is also within the bounds of Article III in its appellate form. The district court had subject matter jurisdiction over this diversity case. Therefore, the Seventh Circuit

is also competent to hear this matter. Second, does this case present an Article III "case or controversy," i.e., do the appellants have standing? Objecting shareholders have consistently been found to have standing to appeal the approval of the compromise of a derivative action. *See* discussion *supra*. Even the Seventh Circuit did not deny that the objectors in the case at bar had standing. *See* 134 F.3d at 876. Thus, there is no constitutional bar to the Seventh Circuit's hearing this appeal.

So, on what authority did the Seventh Circuit conclude that it lacked jurisdiction to hear this appeal? First, the court cited *Marino v. Ortiz*, 484 U.S. 301, 304 (1988). That case, however, is completely inapposite to the one at bar. In *Marino*, non-class members objected to the settlement of a class action without intervening. Not surprisingly, this Court affirmed the lower court's dismissal of their appeal. They had no relationship to the parties or the lawsuit and would not have been barred by *res judicata*. In the present case, objecting shareholders, who are in privity with the parties, *Nathan v. Rowan*, 651 F.2d 1223, 1226 (6th Cir. 1981),[6] have appealed the compromise of a derivative suit. Not only will *res judicata* apply to them, *id.*, but, because they appeared in court in answer to the court's notice to show cause why a settlement should not be approved, they are considered to be "'like a defendant who is summoned by process of court and after an adverse

[6] "[I]n shareholder derivative actions arising under Fed.R.Civ.P. 23.1, parties and their privies include the corporation and all nonparty shareholders." *Id.*

ruling has the right to appeal.'" *Cohen v. Young, supra*, 127 F.2d at 724.[7] There are too many legally important differences between *Marino* and the present case for the former to control the latter.

As further evidence that *Marino* is inapplicable to this case, one need only look at the case relied on by this Court as authority for its ruling: *United States ex rel. Louisiana v. Jack*, 244 U.S. 397, 402 (1917). The *Jack* Court was faced with an appeal of a settlement involving certain real estate by the State of Louisiana after the Supreme Court of Louisiana had held that the state had no interest in the lands in controversy. In other words, the nonintervening objector could not appeal the approval of the settlement because the *governing state law denied it the right to object*. That is the converse of the present case, in which the governing state law specifically gives the objectors the right to appeal, *see* discussion *infra* Part III, and thus cannot control the decision here.

Second, the Seventh Circuit relied on Federal Rule of Appellate Procedure 3(c), which merely provides that, "[a] notice of appeal must specify the party or parties taking the appeal by naming each appellant in either the caption or the body of the notice of appeal." This language is very odd to choose as evidence of a jurisdictional bar, especially in light of this Court's

[7] The Sixth Circuit quoted *Pianta v. H.M. Reich Co.*, 77 F.2d 888, 890 (2d Cir. 1935), which applied the same principle to nonintervening nonparty creditors who wished to challenge the acts of receivers.

conclusion that requiring a nonparty to seek intervention before appealing is simply "the better practice." *Marino*, 484 U.S. at 304. More importantly, however, Rule 3(c), formerly Federal Rule of Civil Procedure 73(b), was promulgated pursuant to the Rules Enabling Act, 28 U.S.C. § 2072, which provides that "[s]uch rule[ ] shall not abridge, enlarge or modify any substantive right." An objecting shareholder in a derivative suit plays an important role, both at the trial and appellate levels, in the vindication of the substantive rights of the corporation. *See* discussion *infra* Parts II, III. Interpreting Rule 3(c) as the Seventh Circuit did eviscerates that role. This Court, when faced with such a choice, has wisely chosen to interpret the Federal Rule narrowly, thus avoiding a conflict with the substantive law. Only two years ago, this Court noted, "Federal courts have interpreted the Federal Rules . . . with sensitivity to important state interests and regulatory policies." *Gasperini, supra*, 518 U.S. at 427 n.7 .[8]

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[8] In *Gasperini*, this Court cited *Walker v. Armco Steel Corp.*, 446 U.S. 740, 750-52 (1980) (reaffirming decision in *Ragan v. Merchants Transfer & Warehouse Co.*, 337 U.S. 530 (1949), that state law rather than Federal Rule of Civil Procedure 3 determines when a diversity action commences for the purposes of tolling the state statute of limitations; Rule 3 makes no reference to the tolling of state limitations, the Court observed, and accordingly found no "direct conflict"); *S.A. Healy Co. v. Milwaukee Metropolitan Sewerage Dist.*, 60 F.3d 305, 310-12 (7th Cir. 1995) (finding state provision for offers of settlement by plaintiffs compatible with Federal Rule of Civil Procedure 68, which is limited to offers by defendants). *See also Cohen v. Beneficial Indus. Loan Corp.*, 337 U.S. 535 (1949) (finding state provision for security for expenses did not conflict with then Rule 23(b), which was silent on the question).

In the present case, it is easy to find an interpretation of Rule 3(c) that does not conflict with the governing substantive law. Delaware law treats objecting shareholders in a Rule 23.1 action to all intents and purposes as parties, *see* discussion *infra* Part III, and, with the sole exception of the Seventh Circuit's opinion in the case at bar, the lower federal courts have done the same, *see* discussion *supra*. Thus, the phrase "party or parties" in Rule 3(c) should be simply interpreted to refer not only to those who are technically parties, but also to those who, like objecting shareholders in a derivative action,[9] are treated as parties by the underlying substantive law.

Moreover, unlike the situations facing this Court in *Byrd v. Blue Ridge Rural Electric Cooperative, Inc.*, 356 U.S. 525 (1958), and *Gasperini*, there is no strong countervailing federal interest here in adopting the Seventh Circuit's new, narrow interpretation of Rule 3(c). When the Rule was originally promulgated in 1938 as Federal Rule of Civil Procedure 73(b), the Advisory Committee's only concern was to abolish the practice of filing assignments of error in the district courts. *See*

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[9] Another example of such a *de facto* party might be a nonintervening nonparty creditor challenging the actions of a receiver. *See supra* note 7.

Fed. R. Civ. P. 73 advisory committee's note. When this Rule was re-promulgated in 1967 as Federal Rule of Appellate Procedure 3(c), the Advisory Committee, noting that the Rule was "identical with corresponding provisions in FRCP 73(b)," stressed only the importance of timeliness in the filing of a notice of appeal. *See* Fed. R. App. P. 3 advisory committee's note. Additionally, this Court has held that

> [t]he purpose of the specificity requirement of Rule 3(c) is to provide notice both to the opposition and to the court of the identity of the *appellant or appellants*. The use of the phrase "et al.," which literally means "and others," utterly fails to provide such notice to either intended recipient. Permitting such vague designation would leave the appellee and the court unable to determine with certitude whether a losing party not named in the notice of appeal should be bound by an adverse judgment or held liable for costs or sanctions.

Torres v. Oakland Scavenger Co., 487 U.S. 312, 318 (1988) (emphasis added). None of these policies would be frustrated, or even slightly affected, by interpreting the phrase "party or parties" to include those treated as parties by the governing substantive law.

Finally, to adopt the Seventh Circuit's unique approach would invite the kind of forum shopping this Court hoped to prevent by its decision in *Erie*. *See Hanna v. Plumer*, 380 U.S. 460, 468 (1965) ("twin aims of the *Erie* rule: discouragement of forum-shopping and

avoidance of inequitable administration of the laws"). In the case at bar, the substantive law provides the role of the objecting shareholder as a check on the very real threat of collusion between plaintiffs' attorneys and defendants in shareholder derivative suits. If Rule 3(c) is interpreted to place such burdens on playing that role that the check will be significantly eroded in federal court (*see* Br. for Barclays Global Investors, State of Wis. Inv. Bd., & Certain Other Inst'l Investors as Amici Curiae Supp'g Pet'rs Part I), given the choice, plaintiffs' attorneys will always choose federal court over state court, thus leading to the inequitable administration of the laws depending on the accident of diversity.

II. THE COURT BELOW UNDERESTIMATED THE SIGNIFICANCE OF THE OBJECTORS' INTEREST IN THE DERIVATIVE ACTION AS A MATTER OF SUBSTANTIVE LAW.

At least tacitly acknowledging the relevance of the position of the stockholder under applicable substantive law, the court below did examine the substantive position of stockholders of a Delaware corporation in relation to a stockholder derivative action. Several of its assertions in this regard, however, were inconsistent with Delaware substantive law. First, the court below asserted that stockholders "may not displace the board in litigation"; second, it asserted that "[s]hareholders have no more the attributes of parties when managers settle derivative litigation than when managers settle antitrust litigation"; and most bluntly and incorrectly, the court below asserted that "shareholders . . . have no more right to speak for the firm or control its litigation decisions than bondholders or banks or

landlords, all of whom have contractual interests that may be affected by litigation." 134 F.3d at 874-76.

This failure to distinguish stockholders from the various other constituencies affected by the disposition of a stockholder derivative action contravenes settled Delaware law defining the stockholder's interest in the control and disposition of the derivative action. Contrary to the assertion of the court below, the stockholders *do* "displace the board in litigation" where a derivative action is allowed to proceed: what they displace, more specifically, is the ordinary prerogative of the board of directors to determine, without stockholder approval or control, whether, when, and how to pursue litigation on behalf of the corporation.[10] Indeed, it is that very characteristic of derivative litigation that has resulted in strict limitations upon the ability of stockholders to initiate derivative actions, in which the ordinary managerial authority of the board of directors over the handling of corporate claims is displaced by stockholder action.[11] See, for example, *Heineman v. Datapoint*

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[10] *Spiegel v. Buntrock*, 571 A.2d 767, 772-73 (Del. 1990); *Zapata Corp. v. Maldonado*, 430 A.2d 779, 782 (Del. 1981) ("Directors of Delaware corporations derive their managerial decision making power, which encompasses decisions whether to initiate, or refrain from entering, litigation, from 8 *Del. C.* §141(a).").

[11] *E.g.*, *Grimes v. Donald*, 673 A.2d 1207, 1215 (Del. 1996) (citing *Pogostin v. Rice*, 480 A.2d 619, 624 (Del. 1984)); *Rales v. Blasband*, 634 A.2d 927, 932 (Del. 1993); *Spiegel v. Buntrock*, 571 A.2d 767, 773 (Del.

Corp., 611 A.2d 950 (Del. 1992), which holds that even though the board of directors ordinarily "makes the ultimate decision of whether or not to prosecute the [corporation's] claim," stockholders may initiate and prosecute the claim derivatively where:

> a reasonable doubt exists that the board has the ability to exercise its managerial power, in relation to the decision to prosecute, within the strictures of its fiduciary obligations.

Id. at 952.

Thus, where the board of directors is considered capable of dealing with the corporation's claim "within the strictures of its fiduciary obligations," the stockholder derivative action must be dismissed for failure to make pre-suit demand. In contrast, where a stockholder derivative action is settled, and not dismissed for failure to make demand upon the board, it is at least implicit, if not explicit, that the plaintiff stockholder has the authority as a matter of substantive corporate law to pursue the action on behalf of the corporation without the approval of the board of directors.[12] In other words,

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1990) (citing *Daily Income Fund, Inc. v. Fox*, 464 U.S. 523, 531 (1984)).

[12] In the instant case, the defendants sought to dismiss the action for failure to make a presuit demand upon the board of directors. The defendants chose to settle the action, however, rather than have the trial court determine their motion to dismiss. By doing so, the

and contrary to the assertion by the court below, the board of directors' power over the conduct of the litigation is displaced. No other constituency—neither the "bondholders or banks or landlords" mentioned in the opinion below—has this power "to speak for the firm [and] control its litigation decisions" that the state substantive law confers upon stockholders. 134 F.3d at 874.

It is true, as the court below observed, 134 F.3d at 875 (citing *Kamen, supra*), that the board of directors may, upon appropriate action, reclaim the power to control the conduct (or dismissal) of a derivative action.[13] Where such power has not been exercised, however, the stockholders are, as a matter of substantive corporate law, *not* strangers to the controversy; to the contrary, they continue to hold the power to conduct the litigation of the corporation's claims. *See, e.g.*, *Levine v. Smith*, 1987 Del. Ch. LEXIS 524, *16-*17 (Del. Ch. 1987), *aff'd*, 591 A.2d 194 (Del. 1991) (when a special litigation committee seeks

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defendants have secured a bar against prosecution of settled claims on behalf of the corporate defendant by anyone, anywhere, rather than simply a dismissal of the plaintiff in this action alone.

[13] *Grimes v. Donald*, 673 A.2d 1207, 1216 n.13 (Del. 1996); *Kaplan v. Wyatt*, 499 A.2d 1184 (Del. 1985); *Zapata Corp. v. Maldonado*, 430 A.2d 779, 785-89 (Del. 1981) (establishing standards for judicial review of special litigation committee motion to terminate stockholder derivative action).

dismissal of the derivative action, "managerial power to control the destiny of the corporation's claim . . . is presumed to be properly vested in the stockholder-plaintiff," and the only issue is whether that power "should in essence be 'revested' in the Board of Directors.").

This substantive law position of stockholders in derivative actions is consistent with the the requirement of both Federal Rule of Civil Procedure 23.1 and Chancery Court Rule 23.1 that the stockholders be given notice of a settlement of a derivative action. That notice requirement reflects a recognition that the stockholders of the corporation have a unique and meaningful interest in the settlement of a derivative action, in contrast to the "employees, vendors, and lawyers" or other persons potentially affected by the settlement of a derivative suit, 134 F.3d at 874, none of whom are required by Rule to be given notice of the settlement. Thus, stockholders who objected to the settlement in this action, unlike members of other corporate constituencies, were invited by the trial court to appear at the settlement hearing to "show cause why the proposed Settlement should not be approved," including submission of "papers and briefs."[14]

Objectors to the settlement of a derivative action are distinguished from members of such other corporate constituencies in a number of additional ways not reflected in Federal Rule of Civil Procedure 23.1, that

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[14] Notice of Hr'g on Proposed Settlement of Derivative Actions, dated May 30, 1997, at 7.

confirm the substantive significance of the stockholders' interest. Notably, stockholders objecting to a proposed settlement of a stockholder derivative action are, unlike nonparties generally, usually afforded access to the discovery process, albeit on a limited basis consistent with the limited scope of the issues presented to the trial court in reviewing the proposed settlement.[15] Moreover, so significant is the interest of the stockholders in the derivative action that final judgments entered in settlement of such actions routinely make explicit that the judgment binds the stockholders individually and precludes them from asserting settled claims.[16] In contrast, we are aware of no judgments in stockholder derivative actions that attempt to operate explicitly and directly upon any other kind of person (employee, vendor, etc.) who may be affected by the judgment.

In sum, the court below failed to acknowledge the

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[15] *See, e.g., Lewis v. Hirsch*, 1995 Del. LEXIS 62, *3 (Del. Ch. 1995). *See generally* Donald J. Wolfe, Jr. & Michael A. Pittenger, *Corporate and Commercial Practice in the Delaware Court of Chancery* § 9-4(g) (1998).

[16] *See* 2 *Business and Commercial Litigation in Federal Courts* 66 (Robert L. Haig, ed. 1998) (model form of order and final judgment). The final judgment entered in this case likewise purports to operate directly on the individual stockholders of the corporation. *See* Petition for Certiorari herein, dated April 21, 1998, Appendix B, ¶7 (releasing claims "by any shareholder of [the] company derivatively on its behalf ... .").

significant role played by stockholders, including objectors to settlements, in the stockholder derivative action. Its assessment of the objectors' entitlement to appeal may thus have rested upon an underestimation of the objectors' substantive position under applicable Delaware law.

III. UNSUCCESSFUL OBJECTORS IN THE DELAWARE COURTS MAY APPEAL SETTLEMENT APPROVALS IN DERIVATIVE ACTIONS WITHOUT FORMAL INTERVENTION.

In Delaware, widely recognized as the predominant jurisdiction of incorporation of corporations the shares of which are publicly traded,[17] including the corporate defendant in this case, the courts have invariably and frequently allowed stockholders who have objected to the settlement of a derivative action, but who have not intervened as parties in the action, to appeal the approval of the settlement by the trial court, the Delaware Court of Chancery.

Nearly fifty years ago, the Delaware Supreme Court faced the very question now before this Court. *Braun v. Fleming-Hall Tobacco Co., Inc.*, 92 A.2d 302 (Del. 1952). The proponents of the settlement of a

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[17] According to the Division of Corporations of the Secretary of State of the State of Delaware, 60% of the Fortune 500 companies are incorporated in Delaware, and 50% of the corporations with shares listed on the New York Stock Exchange are incorporated in Delaware. <http://www.state.de.us/corp.index.html>.

stockholder derivative action sought to dismiss an objecting stockholder's appeal of the trial court's approval of the settlement on the ground, among others, that the objector "had not obtained an order granting him leave to intervene as a party." *Id.* at 307. The Delaware Supreme Court at first acknowledged that such intervention had been "the practice" of persons objecting to settlements. *Id.* at 308. Despite that recognition, however, the court found the nonintervening objector entitled to appeal approval of the settlement, reasoning:

> [The objector] was under a rule to appear before the Court of Chancery if he considered his interests in jeopardy; and it was pursuant to that rule that his counsel filed written objections to the settlement and made oral argument against the approval thereof. Nobody objected to either of these activities in the trial court. *What took place, therefore, amounted to actual intervention, even though it was without express leave of court.* If counsel for [the objector] had asked to intervene, an order granting leave would undoubtedly have been entered. *In these circumstances, therefore, we do not regard the failure to ask permission to intervene as any more than the oversight of a formality.*

Id. (emphasis added).

In the half century or so since *Braun* was decided, what the court described as "the oversight of a formality" has become common practice: objectors almost invariably assert their position without intervening formally, and the Delaware Supreme Court has never

once questioned the ruling in *Braun* that this approach does not preclude appeal by an unsuccessful objector.[18] To the contrary, that court has repeatedly entertained, on the merits, appeals by objectors to settlements of derivative actions, despite their not having intervened as parties. *Gladstone v. Bennett*, 153 A.2d 577 (Del. 1959); *Krinsky v. Helfand*, 156 A.2d 90 (Del. 1959); *Rome v. Archer*, 197 A.2d 49 (Del. 1964); *Hoffmann v. Dann*, 205 A.2d 343 (Del. 1964); *Goodman v. Futrovsky*, 213 A.2d 899 (Del. 1965); *Rutman v.Kaminsky*, 226 A.2d 122 (Del. 1967); *Neponsit Investment Co. v. Abramson*, 405 A.2d 97 (Del. 1979); *Geller v. Tabas*, 462 A.2d 1078 (Del. 1983) (noting that objectors who had brought separate suit in another State had made no attempt to intervene in the Delaware action, but ruling on the merits of objectors' appeal from approval of the settlement); *Polk v. Good*, 506 A.2d 531 (Del. 1986) (at time of approving the settlement, the Court of Chancery had denied objectors' motions to intervene, and appellate review addressed the merits of the objections without comment on the intervention ruling).

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[18] Similarly, stockholders routinely submit objections to proposed settlements in the Court of Chancery without seeking formal leave to intervene as a party. *E.g.*, *Cohan v. Loucks*, 1993 WL 121855 (Del. Ch. 1993); *Stepak v. Ross*, 1985 WL 21137 (Del. Ch. 1985); *Moses v. Pickens*, 1982 WL 17825 (Del. Ch. 1982); *Lewis v. Fuqua Industries, Inc.*, 1982 WL 8783 (Del. Ch. 1982); *Saminsky v. Abbott*, 194 A.2d 549 (Del. Ch. 1963); *Manacher v. Reynolds*, 165 A.2d 741 (Del. Ch. 1960).

This Delaware practice of allowing appeals by nonintervening objecting stockholders in derivative actions has continued unabated after this Court's decision in *Marino*. In *In re Resorts Int'l Shareholder Litigation Appeals*, 570 A.2d 259 (Del. 1990), one of several objectors to the settlement of a class and derivative action filed separate suit, shortly after filing of the settlement agreement, but none of the objectors sought to intervene in the action in which the settlement was submitted. The Delaware Supreme Court proceeded to rule on the merits of the appeal, notwithstanding that failure to intervene. Similarly, in *Kahn v. Sullivan*, 594 A.2d 48 (Del. 1991), California Public Employees Retirement System (CalPERS, one of the appellants in this case) had intervened in an action challenging conduct of Armand Hammer, the chief executive officer of Occidental Petroleum Corporation, a Delaware corporation, in relation to the funding of a museum to house Mr. Hammer's extensive art collection. In a separate derivative action (the Sullivan action) in the Delaware Court of Chancery addressing the same alleged misconduct, the parties agreed to a settlement and presented it for approval at a hearing on notice to the other Occidental stockholders, including CalPERS. *Without having intervened in the Sullivan action*, CalPERS submitted objections to the settlement, and appealed the approval of the settlement to the Delaware Supreme Court. That court entertained the appeal without any suggestion that CalPERS should have intervened in the action in which the settlement was

approved.[19]

CONCLUSION

For the reasons set forth above, we respectfully submit that the decision of the court below, denying the right of appeal to a stockholder who duly objects to a proposed settlement of a stockholder derivative action, is inconsistent with pertinent state law and practice. In order to give effect to the underlying substantive law of the state of incorporation, here Delaware, this Court should determine that the petitioners, who duly objected to a proposed settlement of a stockholder derivative action arising under and governed by Delaware law, are entitled to appeal the trial court's approval of the settlement, notwithstanding any failure to intervene as parties under Federal Rule of Civil Procedure 24.

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[19] *Kahn v. Sullivan* is thus similar to *Prezant v. DeAngelis*, 636 A.2d 915 (Del. 1994), a case noted extensively by this Court in *Matsushita Elec. Indus. Ltd. v. Epstein*, 516 U.S. 367 (1996). In *Prezant*—a class action—the objector had filed a separate action, but submitted objections to a settlement without intervening in the case in which the settlement was approved. After approval of the settlement, the objector appealed—successfully—to the Delaware Supreme Court, again without any suggestion that intervention was necessary to the appeal.

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IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1998

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM AND FLORIDA STATE BOARD OF ADMINISTRATION,
Petitioners,

v.

PAUL FELZEN, *et al.*,
Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF OF *AMICUS CURIAE* COUNCIL OF INSTITUTIONAL INVESTORS IN SUPPORT OF PETITIONERS

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2918

QUESTION PRESENTED

Whether a shareholder who, pursuant to Federal Rule of Civil Procedure 23.1, appears in federal district court and presents objections to a proposed dismissal or settlement of a derivative action, must also intervene pursuant to Federal Rule of Civil Procedure 24 to appeal an adverse decision.

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES iv

INTEREST OF *AMICUS CURIAE* 1

SUMMARY OF ARGUMENT 2

ARGUMENT 4

I. OBJECTING SHAREHOLDERS PLAY A VALUABLE ROLE IN ENSURING THE FAIRNESS AND INTEGRITY OF SETTLEMENTS IN SHAREHOLDER DERIVATIVE LITIGATION . 4

A. The Settlement of Shareholder Derivative Actions Is Fraught With Potential for Conflict of Interest and Unfairness 5

B. Objecting Shareholders Are Essential to Ensuring Fairness in Derivative Settlements 11

II. REQUIRING SHAREHOLDER OBJECTORS TO INTERVENE TO OBTAIN APPELLATE REVIEW WOULD HINDER EFFECTIVE MONITORING OF DERIVATIVE SUIT SETTLEMENTS 16

A. Appellate Review of Shareholders' Objections Is Essential to the Effective Monitoring of Derivative Suit Settlements 17

B. Requiring Intervention to Secure the Right to Appeal Would Cut Off Appellate Review of Some Derivative Settlements and Erect Unfair and Unnecessary Barriers to Effective Policing of Others 21

1. An Intervention Requirement Would Unduly Limit and Increase the Costs of Appeals by Shareholder Objectors 21

2. An Intervention Requirement Would Provide No Corresponding Benefit 26

CONCLUSION 29

TABLE OF AUTHORITIES

CASES

Alleghany Corp. v. *Kirby*,
333 F.2d 327 (2d Cir. 1964), *aff'd en banc by an equally divided court*,
340 F.2d 311 (2d Cir. 1965) 7,12,15

Bell Atlantic Corp. v. *Bolger*,
2 F.3d 1304 (3d Cir. 1993) ..... *passim*

Braun v. *Fleming-Hall Tobacco Co.*,
92 A.2d 302 (Del. Ch. 1952) 27

Burks v. *Lasker*,
441 U.S. 471 (1979) 7,11

In re Chambers Dev. Sec. Litig.,
912 F. Supp. 822 (W.D. Pa. 1995) 15,20

City of Detroit v. *Grinnell Corp.*,
495 F.2d 448 (2d Cir. 1974) 20

Cohen v. *Beneficial Indus. Loan Corp.*,
337 U.S. 541 (1949) 4,5,6,7

Cohen v. *Young*,
127 F.2d 721 (6th Cir. 1942) 13

Daily Income Fund, Inc. v. *Fox*,
464 U.S. 523 (1984) 11

Dietrich Corp. v. *King Resources Co.*,
596 F.2d 422 (10th Cir. 1979) 27,28

Ficalora v. *Lockheed Cal. Co.*,
751 F.2d 995 (9th Cir. 1985) 20

In re General Motors Corp. Engine Interchange Litig.,
594 F.2d 1106 (7th Cir. 1979) 20

In re General Motors Corp. Pick-Up Truck Fuel Tank Prods. Liab. Litig.,
55 F.3d 768 (3d Cir. 1995) 19

In re General Tire & Rubber Co. Sec. Litig.,
726 F.2d 1075 (6th Cir. 1984) 26

Girsh v. *Jepson*,
521 F.2d 153 (3d Cir. 1975) 11,13,19

Gluck v. *Cellstar Corp.*,
976 F. Supp. 542 (N.D. Tex. 1997) 25

Greenfield v. *Villager Indus., Inc.*,
483 F.2d 824 (3d Cir. 1973) 7

Greenspun v. *Bogan*,
492 F.2d 375 (1st Cir. 1974) 13

Kamen v. *Kemper Finan. Servs.*,
500 U.S. 90 (1991) 5

Lipscomb v. *Wise*,
643 F.2d 319 (5th Cir. 1981) 27,28

Malchman v. *Davis*,
706 F.2d 426 (2d Cir. 1983) 20

In re Oracle Sec. Litig.,
829 F. Supp. 1176 (N.D. Cal. 1993) 12

In re Pacific Enters. Sec. Litig.,
47 F.3d 373 (9th Cir. 1995) 15,20

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543 F.2d 1058 (3d Cir. 1976) 18,19,27

Ragsdale v. *Turnock*,
941 F.2d 501 (7th Cir. 1991) 23

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64 F.3d 1439 (10th Cir. 1995) ..... *passim*

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78 F.R.D. 150 (S.D.N.Y. 1978) 22

Saylor v. *Lindsley*,
456 F.2d 896 (2d Cir. 1972) 8,9,10

Seigal v. *Merrick*,
619 F.2d 160 (2d Cir. 1980) 16

Strawbridge v. *Curtis*,
7 U.S. (3 Cranch) 267 (1806) 22

Stromberg Metal Works v. *Comfort Control, Inc.*,
77 F.3d 928 (7th Cir. 1996) 22

Thompson v. *Freeman*,
648 F.2d 1144 (8th Cir. 1981) 27

Tryforos v. *Icarian Dev. Co.*,
518 F.2d 1258 (7th Cir. 1975) 27

Turner/Ozanne v. *Hyman/Power*,
111 F.3d 1312 (7th Cir. 1997) 22

United States Catholic Conference v. *Abortion Rights Mobilization, Inc.*,
487 U.S. 72 (1988) 27

In re Urcarco Sec. Litig.,
148 F.R.D. 561 (N.D. Tex. 1993) 10

In re Warner Communications Sec. Litig.,
618 F. Supp. 735 (S.D.N.Y. 1985), *aff'd*,
798 F.2d 23 (2d Cir. 1986) 13

In re Wells Fargo Sec. Litig.,
991 F. Supp. 1193 (N.D. Cal. 1998) 2

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800 F.2d 386 (4th Cir. 1986) 15

STATUTES & RULES

Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, 109 Stat. 737 (1995) 25

28 U.S.C. § 1367(b) 22

42 U.S.C. § 1973*l*(e) 28

Fed. R. Civ. P. 23.1 4,11,21,23,24

24(a) 23

24(c) 23

26(b) 24

LEGISLATIVE HISTORY

Private Securities Litigation Reform Act of 1995, H.R. 104-98 at 32, *reprinted in* 1995 U.S.C.C.A.N. 679, 731 10

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§ 1909 23

5A § 3902.1 27

IN THE
SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1998

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM AND FLORIDA STATE BOARD OF ADMINISTRATION,
Petitioners,

v.

PAUL FELZEN, *et al.*,
Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF OF *AMICUS CURIAE* COUNCIL OF INSTITUTIONAL INVESTORS IN SUPPORT OF PETITIONERS

INTEREST OF *AMICUS CURIAE*[1]

The Council of Institutional Investors (the "Council") is an organization of public, Taft-Hartley and corporate pension funds that seeks to address investment issues that affect the security of pension plan assets by encouraging institutional investors to take an active role in protecting those assets. The Council was founded in 1985 in response to controversial takeover activities that threatened the financial interests of

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[1] Pursuant to Rule 37.6 of the Rules of this Court, *amicus* states that no counsel for a party authored this brief in whole or in part, and no person or entity other than *amicus* and their counsel made any monetary contribution to the preparation or submission of this brief. Pursuant to Rule 37.3, *amicus* states that petitioners and respondents have granted consent to file this brief.

pension fund beneficiaries. Since that time, the Council has grown to over 100 members who control pension assets in excess of $1 trillion and represent millions of plan beneficiaries and participants. The Council is recognized as a significant voice for investors on issues of corporate governance, executive compensation, and corporate accountability to shareholders, see, *e.g.*, *In re Wells Fargo Sec. Litig.*, 991 F. Supp. 1193, 1198 (N.D. Cal. 1998), and consistently has been a proponent of meaningful shareholder participation in major decisions that affect corporate viability.

The interests of the Council are directly implicated by this case. Consistent with its view that participation by shareholders in corporate decision making generally provides substantial benefits, the Council believes that such participation is essential to judicial assessment of the fairness of voluntary settlements in shareholder derivative actions. The Council believes that the decision below, if affirmed, would erect a substantial and unnecessary barrier to full participation by objecting shareholders in the review of proposed settlements in cases where such participation is most needed.

SUMMARY OF ARGUMENT

Shareholder objectors who appear before district courts to voice concerns regarding proposed settlements in shareholder derivative actions under Federal Rule of Civil Procedure 23.1 ("Rule 23.1") play an important role in policing the fairness of such settlements and should not be required to intervene as named plaintiffs to secure a right to appeal the rejection of their objections. Rule 23.1, settled precedent, and substantial legal commentary confirm that shareholder derivative actions are subject to unusual conflicts of interest that frequently undermine confidence that a proposed voluntary compromise is in the best interests of the corporation. The requirement of mandatory

"notice" to shareholders of a proposed settlement and their subsequent participation in the settlement process provides an important check against collusive or otherwise improper settlements. Indeed, when objecting shareholders' views have been given studied consideration, they have resulted in substantial modifications of settlement proposals that provided tangible benefits to the corporation. All too often, however, valid shareholder objections may be ignored or improperly rejected by district courts that are denied a full adversarial presentation by the named parties and operating under a strong incentive to approve quick settlements.

Under these circumstances, appellate review is an essential component of effective shareholder participation. It provides a direct avenue for correcting district court errors and a strong incentive for district courts to consider shareholder objections fully and fairly in the first instance. In contrast, denying or discouraging appeals by objecting shareholders would insulate erroneous decisions from review and would strengthen the incentive of district courts to disregard shareholder objections. A requirement of intervention under Federal Rule of Civil Procedure 24 would produce precisely these untoward effects. If such a requirement were imposed, some shareholder objectors would be unable to intervene and would therefore be shut off from appellate review. The remainder would be saddled with substantial additional costs and burdens that create no corresponding benefit to the litigation. Imposition of such a requirement would thus limit participation by shareholder objectors and thereby undermine the fairness of these settlements.

ARGUMENT

I. OBJECTING SHAREHOLDERS PLAY A VALUABLE ROLE IN ENSURING THE FAIRNESS AND INTEGRITY OF SETTLEMENTS IN SHAREHOLDER DERIVATIVE LITIGATION.

Rule 23.1 governs the conduct of derivative actions by shareholders in federal courts and provides, in pertinent part:

> The derivative action may not be maintained if it appears that the *plaintiff does not fairly and adequately represent the interests of the shareholders or members similarly situated in enforcing the right of the corporation or association*. The action shall not be dismissed without the approval of the court, and *notice of the proposed dismissal or compromise shall be given to shareholders* or members in such manner as the court directs.

Id. (emphasis added). As the language of Rule 23.1 confirms, its drafters were aware that shareholder derivative actions are susceptible to conflicting and divergent interests arising between the named plaintiff (or plaintiff's counsel) and the corporation (or similarly situated shareholders) on whose behalf the named plaintiff purports to act. These concerns are amplified in the context of voluntary settlements. When derivative claims are compromised, the suing stockholder may face strong financial incentives to "sell out" the interests of the corporation in return for "payments from corporate assets" to plaintiff's counsel, who often act as the controlling force in derivative litigation. *Cohen* v. *Beneficial Indus. Loan Corp.*, 337 U.S. 541, 548 (1949). To police that potential for abuse, Rule 23.1 requires district court approval of any such settlement and provides that notice of a proposed compromise "shall" be provided to shareholders

before the district court considers the merits of the settlement proposal. The notice requirement is designed to ensure that settlements will not be approved without giving shareholders an opportunity to object. Such objections provide an important corrective to the often considerable momentum behind proposed derivative settlements and frequently result in substantial enhancements to the fairness and value of such settlements.

A. The Settlement of Shareholder Derivative Actions Is Fraught With Potential for Conflict of Interest and Unfairness.

From the time of its earliest recognition in the United States, both the relative merits and the potential abuses of shareholder derivative litigation have been the subject of discussion by courts, legislatures, and legal commentators. As this Court explained nearly a half century ago, the shareholder derivative suit arose at a time when "[c]orporate laws were lax and were not self-enforcing, and stockholders, in face of gravest abuses, were singularly impotent in obtaining redress of abuses of trust." *Cohen*, 337 U.S. at 547-48. Responding to this void in legal remedies, "[e]quity came to the relief of the stockholder, who had no standing to bring civil action at law against faithless directors and managers," *id.* at 548, by allowing individual shareholders "to bring suit to enforce a corporate cause of action against officers, directors, and third parties," *Kamen* v. *Kemper Fin. Servs.*, 500 U.S. 90, 95 (1991) (internal quotation marks omitted). By placing litigation authority in the hands of the individual shareholder, the derivative action became "the chief regulator of corporate management and has afforded no

small incentive to avoid at least grosser forms of betrayal of stockholders' interests." *Cohen*, 337 U.S. at 548.[2]

As the *Cohen* Court also noted, however, "the remedy itself provided opportunity for abuse, which was not neglected." *Id.* Enabling individual shareholders to "represent" and act on behalf of the corporation and other shareholders created the risk that the interests of the named plaintiff shareholders would diverge from the interests of the corporation and the other (*de facto* party) shareholders. In some cases, the individual plaintiff could "becom[e] faint hearted prior to the litigation's completion and would be willing to settle the action even though it might not be in the best interests of all concerned." 7C Charles Alan Wright *et al.*, *Federal Practice & Procedure* § 1839, at 177 (1986) (citing *Webster Eisenlohr, Inc.* v. *Kalodner*, 145 F.2d 316, 320 (3d Cir. 1944)).

In the worst cases, the shareholder plaintiff might enter into "secret settlements in which any wrongs to the general body of share owners were compounded by the suing stockholder, who

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[2] *See also* 13 William Meade Fletcher, *Cyclopedia Corporations* § 5940, at 26 (1995) ("The derivative proceeding developed as an equitable device to enable shareholders to enforce a corporate right against faithless officers and directors . . . that the corporation had either failed or refused to assert on its own"); Ralph C. Ferrara *et al.*, *Shareholder Derivative* Litigation § 1.03, at 1-14 (1995) ("Equity came to the relief of the stockholder, [and] . . . allowed him to step into the corporation's shoes and seek, on behalf of the corporation, the restitution he could not demand on his own."); Bert S. Prunty, *The Shareholders' Derivative Suit: Notes on Its Derivation*, 32 N.Y.U. L. Rev. 980, 980 (1957) ("The story of the derivative suit in its infancy and adolescence is that of the lawmakers' response to recognized misuse of economic organizations viewed against popularly accepted standards of business conduct. The shareholders' right to command a judicial forum comes in answer to a demonstration of need.").

was mollified by payments from corporate assets." *Cohen*, 337 U.S. at 548. As Judge Friendly explained:

> The plaintiff stockholders . . . have every incentive to accept a settlement that runs into high six figures or more regardless of how strong the claims for much larger amounts may be . . . . [A] juicy bird in the hand is worth more than the vision of a much larger one in the bush, attainable only after years of effort not currently compensated and possibly a mirage.

Alleghany Corp. v. *Kirby*, 333 F.2d 327, 347 (2d Cir. 1964) (Friendly, J., dissenting), *aff'd en banc by an equally divided court*, 340 F.2d 311 (2d Cir. 1965). Given these dynamics, special care is warranted in the conduct and oversight of derivative actions "to prevent plaintiffs from selling out their fellow shareholders." *Burks* v. *Lasker*, 441 U.S. 471, 485 n.16 (1979).[3]

The potential for collusion, conflict of interest or agency problems is especially acute in derivative litigation because of the unusual degree to which plaintiff's counsel, rather than the plaintiff, controls and directs the course of such litigation. See *Greenfield* v. *Villager Indus., Inc.*, 483 F.2d 824, 832 n.8 (3d Cir. 1973) ("[C]ounsel for the class representative and not the

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[3] *See also* 7C Charles Alan Wright *et al.*, *Federal Practice & Procedure* § 1839, at 177 (1986) ("Special caution is warranted in the context of derivative suits inasmuch as plaintiff is affecting a right that belongs to the corporation."); 13 William Meade Fletcher, *Cyclopedia Corporations* § 6020, at 303 (1995) ("The requirement of court approval is intended to protect the interests of other shareholders . . . by prohibiting derivative plaintiffs . . . from settling with defendants for their own personal interests.").

named parties . . . direct and manage these actions").[4] Indeed, "[o]ne of the risks flowing from shareholders' difficulty in monitoring derivative litigation is that plaintiffs' counsel and the defendants will structure a settlement such that the plaintiffs' attorneys' fees are disproportionate to any relief obtained for the corporation" and thereby "settle in a manner adverse to the interests of the plaintiffs by exchanging a low settlement for high fees." *Bell Atlantic Corp.* v. *Bolger*, 2 F.3d 1304, 1310 (3d Cir. 1993). Moreover, in a derivative action, "both sides have a right to be reimbursed their legal expenses when there is a settlement, but not when there is an adverse judgment. These rules obviously create strong pressure for settlement and explain why even a plainly frivolous action may sometimes be settled." John C. Coffee, Jr., *The Unfaithful Champion: The Plaintiff as Monitor in Shareholder Litigation*, 48 Law & Contemp. Probs. 5, 24 (1985).[5]

Commentators agree that such conflicts of interest create the "risk that the representative plaintiff will collude with the defendant to forgo the derivative claims in exchange for a settlement that is only favorable to the representative plaintiff

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[4] *See* Daniel R. Fischel & Michael Bradley, *The Role of Liability Rules and the Derivative Suit in Corporate Law*, 71 Cornell L. Rev. 261, 271 & n.26 (1986) (noting that the "real party in interest is the attorney"); *cf.* Deborah L. Rhode, *Class Conflicts in Class Actions*, 34 Stan. L. Rev. 1183, 1203 (1982) ("[A]s a practical matter, once a class is certified, named plaintiffs generally are neither highly motivated nor well situated to monitor the congruence between counsel's conduct and class preferences.").

[5] *See also Saylor* v. *Lindsley*, 456 F.2d 896, 900 (2d Cir. 1972) (noting fact that "[a] relatively small settlement may well produce an allowance bearing a higher ratio to the cost of the work than a much larger recovery obtained only after extensive discovery, a long trial and an appeal," thereby creating the danger that a plaintiffs' attorney will settle a derivative claim for less than its expected value in return for this proportionately higher fee "allowance").

and his or her attorneys." 5 *Moore's Federal Practice* § 23.1.10[2][a], at 23.1-58 (1998); see also 7C Charles Alan Wright *et al.*, *Federal Practice & Procedure* § 1839, at 191 ("[T]he Court should be on the lookout for signs of bad faith or collusion among the parties to the proposed settlement."). As one commentator described the problem:

> [E]ffective control is almost entirely in the hands of the attorney. The most obvious examples of attorney control are class actions and shareholder derivative suits, in which the named plaintiff figures only in a symbolic capacity. Such litigation is almost always brought by entrepreneurial lawyers in hopes of obtaining an award of attorney's fees. The attorney exercises virtually plenary control over the litigation, including the decision whether to settle.

Geoffrey P. Miller, *Some Agency Problems in Settlement*, 16 J. Legal Stud. 189, 213-14 (1987); see also Ralph K. Winter, *Paying Lawyers, Empowering Prosecutors, and Protecting Managers: Raising the Cost of Capital in America*, 42 Duke L.J. 945, 948 (1993) ("[P]laintiffs [in derivative and class actions] are generally figureheads . . . because the real incentive for bringing such actions is the quest for attorney's fees.").

Assumption of control over the litigation by plaintiffs' attorneys creates an additional risk in the context of settlement of a shareholder derivative suit because "[t]here can be no blinking at the fact that the interests of the plaintiff in a stockholder's derivative suit and of his attorney are by no means congruent." *Saylor* v. *Lindsley*, 456 F.3d 896, 900 (2d Cir. 1972). The risks faced by plaintiff and his attorney in proceeding to trial vary substantially because "[f]or the plaintiff, a defendant's judgment may mean simply the defeat of an expectation, often of relatively small amount; for his lawyer it

can mean the loss of years of costly effort by himself and his staff." *Id.* at 900-01. Commentators and scholars uniformly acknowledge this substantial danger of conflicting interests between shareholder plaintiffs and their counsel in the settlement context.[6]

The danger that a proposed settlement will not be in the best interests of the corporation, or even of the named plaintiffs, is further threatened because, as federal legislators have recognized, such cases increasingly are dominated by a small cartel of law firms that recruit "[p]rofessional plaintiffs who own a nominal number of shares in a wide array of public companies" and have no real interest in monitoring their attorney's litigation decisions. See Private Securities Litigation Reform Act of 1995, H.R. 104-98, at 32, *reprinted in* 1995 U.S.C.C.A.N. 679, 731; see also *In re Urcarco Sec. Litig.*, 148 F.R.D. 561, 563 (N.D. Tex. 1993) (noting that plaintiffs "have among their ranks one of the unluckiest and most victimized investors in the history of the securities business"); Deborah A. Demott, *Shareholder Derivative Actions* § 1.05, at 1-13 ("A striking feature of derivative litigation in the post-Depression era is the frequency with which the same plaintiffs make their appearance.").

For these reasons, the settlement of shareholder derivative actions must be closely monitored to ensure that the terms of

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[6] *See* Deborah A. Demott, *Shareholder Derivative Actions* § 7.05, at 7-27 (1994) ("The potential divergence in interests between the plaintiff and the plaintiff's attorney is most likely to materialize in the settlement context."); John C. Coffee, Jr., *Understanding The Plaintiff's Attorney: The Implications of Economic Theory for Private Enforcement of Law Through Class and Derivative Actions*, 86 Colum. L. Rev. 669, 677-78 (1986) (arguing that the client in a derivative suit "generally has only a nominal stake in the outcome of litigation" and cannot closely monitor and control his attorney's conduct).

the proposed settlements are fair and meaningful, and not the product of improper collusion or conflicts of interests.

B. Objecting Shareholders Are Essential to Ensuring Fairness in Derivative Settlements.

Rule 23.1 provides two institutional safeguards designed to protect shareholders' interests from the acute potential for abuse inherent in derivative settlements: (1) district court approval of settlements, and (2) the opportunity for shareholders to raise objections to the proposed settlement.[7] Although the requirement of district court approval stands as a bulwark against improper settlement of derivative actions, Rule 23.1 recognizes that the district court's judgment should be informed by the views of shareholders who have a concrete stake in the resolution of the derivative action. As this Court has recognized, the *dual* requirements of district court approval and notice to shareholders are "intended to prevent plaintiffs from selling out their fellow shareholders," *Burks*, 441 U.S. at 485 n.16, and to prevent circumstances "where the action would disserve the legitimate interests of the company or its shareholders," *Daily Income Fund, Inc.* v. *Fox*, 464 U.S. 523, 532 n.7 (1984).

Thus, under Rule 23.1, the district court has a duty to determine whether the proposed compromise reasonably protects the interests of the corporation and its shareholders. See, *e.g.*, *Girsh* v. *Jepson*, 521 F.2d 153, 157 (3d Cir. 1975) (holding that the district court has a responsibility to assess the interests of the corporation when reviewing a proposed

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[7] *See* Fed. R. Civ. P. 23.1 ("The action shall not be dismissed without the approval of the court, and notice of the proposed dismissal or compromise shall be given to shareholders or members in such manner as the court directs.").

compromise). There are institutional reasons, however, why a district court may be poorly situated to fulfill this duty on its own.

First, the parties to the proposed settlement are unlikely to present "an unbiased portrayal of the merits of the derivative claims." *In re Oracle Sec. Litig.*, 829 F. Supp. 1176, 1185 (N.D. Cal. 1993). Indeed, "[t]he effort to obtain court approval entails the suspension, if not the termination, of hostilities" thereby depriving the district court of "the full benefit of the adversarial process." *Bolger*, 2 F.3d at 1310. The "presentation of plaintiffs' counsel [may be] biased because the settlement offers them a substantial fee, regardless of the benefit conferred on the corporation and its shareholders," while the "presentation on behalf of the [defendants may be] similarly biased in favor of settlement, because the settlement absolves them of liability without requiring them to part with any return consideration." *Oracle*, 829 F. Supp. at 1185. As a result, rather than providing to the district court a full and fair airing of issues occasioned by the settlement, "plaintiffs' attorneys' and defendants' interests coalesce and mutual interest may result in mutual indulgence" whereby the parties "spotlight the proposal's strengths and slight its defects." *Bolger*, 2 F.3d at 1310.[8]

Second, in considering a settlement proposal, a district court may have relatively limited knowledge of the underlying

[8] "Once a settlement is agreed, the attorneys for the plaintiff stockholders link arms with their former adversaries to defend their joint handiwork." *Alleghany Corp.*, 333 F.2d at 346-48 (Friendly, J., dissenting); *see also* Elliot J. Weiss & John S. Beckerman, *Let the Money Do the Monitoring: How Institutional Investors Can Reduce Agency Costs in Securities Class Actions*, 104 Yale L.J. 2053, 2066 (1995) (arguing that district court "settlement hearings typically are not adversarial in character").

action, derived solely from the pleadings and the few briefs that may have been filed prior to settlement discussions. This lack of information makes it difficult for the district court to assess whether the proposed settlement is in the best interests of the corporation. Accordingly, settled precedent prohibits a district court from approving a settlement based "solely on the advice of the attorneys before it." 7C Charles Alan Wright *et al.*, *Federal Practice & Procedure* § 1839, at 186; see also *Greenspun* v. *Bogan*, 492 F.2d 375, 378 (1st Cir. 1974) ("It is well established that a court should not merely rubber stamp whatever settlement is proposed by the parties to a shareholder derivative action."); *Cohen* v. *Young*, 127 F.2d 721, 725 (6th Cir. 1942) ("The rule provides for notice to shareholders . . . in order that the court may have the benefit of that broader information.").

Third, there is a strong institutional bias in favor of settlement. Many courts proceed "from the familiar axiom that a bad settlement is almost always better than a good trial," and therefore may pay inadequate attention to shareholder objectors. *In re Warner Communications Sec. Litig.*, 618 F. Supp. 735, 740 (S.D.N.Y. 1985), *aff'd*, 798 F.2d 25 (2d Cir. 1986). Because "judges generally feel pressured to move their dockets," they have an interest in approving settlements that is at odds with their duty to carefully consider objections and closely scrutinize the fairness of a settlement. Elliot J. Weiss & John S. Beckerman, *Let the Money Do the Monitoring: How Institutional Investors Can Reduce Agency Costs in Securities Class Actions*, 104 Yale L.J. 2053, 2067 (1995); see *Girsh*, 521 F.2d at 157 (reversing district court where objector denied the ability to develop and present her objections to the settlement proposal). Empirical studies reflect that the median lengths of fairness hearings in the two districts for which data were available were, respectively, 38 and 40 minutes. John C. Coffee, Jr., *Class Wars: The Dilemma of the Mass Tort Class*

Action, 95 Colum. L. Rev. 1343, 1348 & n.14 (1995) (arguing that empirical evidence suggests that "courts have little ability or incentive to resist [proposed] settlements"). The typical brevity of these hearings "seems inconsistent with careful judicial scrutiny of the settlement's fairness," *id.* at 1348 n.14, or of the often complex issues raised by objections.

The choices and incentives faced by the district court are straightforward:

> Judges' calendars are crowded with cases, and despite various reform efforts, the workload only seems to increase. If the judge approves the settlement, the result will be to remove a potentially complex and time-consuming case from the judge's calendar; if she rejects it she faces a substantial probability of further litigation.

Jonathan R. Macey & Geoffrey P. Miller, *The Plaintiffs' Attorney's Role in Class Action & Derivative Litigation: Economic Analysis and Recommendations for Reform*, 58 U. Chi. L. Rev. 1, 45-46 (1991). As a result, for some district courts, "settlement hearings are typically pep rallies jointly orchestrated by plaintiffs' counsel and defense counsel" where the district courts "engage in paeans of praise for counsel or lambaste anyone rash enough to object to the settlement." *Id.* at 46-47.

These problems explain why shareholder objectors "play an important role by giving courts access to information on the settlement's merits," and help to compensate for the institutional weaknesses that can blind the district court to an unfair settlement. *Bolger*, 2 F.3d at 1310; see also Deborah A. Demott, *Shareholder Derivative Actions* § 7:01, at 7-4 ("[O]bjectors to the settlement . . . may call the court's attention

to deficiencies that are not likely to be highlighted by the settlement's proponents."); *cf.* Federal Judicial Center, *Empirical Study of Class Actions in Four Federal District Courts: Final Report to the Advisory Committee on Civil Rules* 58 (1996) ("Objections represent an outside source of information about the substance of the settlement and its impact on class members. The settling parties at this stage have little or no incentive to present negative information about the settlement, so objections from class members and others may be a crucial source of information about defects in the settlement."). Indeed, even where there is little or no response by shareholder objectors, that inaction itself provides the court with additional information regarding the settlement's fairness. See *In re Chambers Dev. Sec. Litig.*, 912 F. Supp. 822, 841 (W.D. Pa. 1995) ("The mild response of the class is a factor in favor of settlement on the terms proposed.").[9]

Thus, it is not surprising that the efforts of non-party shareholder objectors in a wide variety of cases have resulted "in significant improvement of the settlement." William L. Cary & Melvin A. Eisenberg, *Corporations* 1057 (1988). For example, in *In re Pacific Enters. Sec. Litig.*, 47 F.3d 373 (9th Cir. 1995), shareholders joined an objection to a proposed settlement with the result that the district court "ultimately lowered the attorneys' fee award from $8 million to $4 million." *Id.* at 375, 377. Similarly, in *Alleghany Corp.*, 333 F.2d at 331-32, an objecting shareholder brought critical information and arguments to the district court's attention, resulting in an increase of the settlement amount from $1 million to $3 million. And, in *Rosenbaum* v. *MacAllister*, 64 F.3d 1439 (10th Cir.

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[9] *Accord Bolger*, 2 F.3d at 1313-14; *Zimmerman* v. *Bell*, 800 F.2d 386, 391 (4th Cir. 1986); Deborah A. Demott, *Shareholder Derivative Actions* § 7.02, at 7-7; Ralph C. Ferrara *et al.*, *Shareholder Derivative Litigation* § 14.05[2], at 14-23.

1995), a shareholder objector was successful in obtaining the reversal of an attorneys' fee award "equal to more than $900 per hour for every attorney, paralegal, and law clerk who worked on the case." *Id.* at 1447-48. These and other representative cases reflect that shareholder objectors make tangible and important contributions to the fairness of derivative settlements when their views are given proper consideration by the district court.[10]

II. REQUIRING SHAREHOLDER OBJECTORS TO INTERVENE TO OBTAIN APPELLATE REVIEW WOULD HINDER EFFECTIVE MONITORING OF DERIVATIVE SUIT SETTLEMENTS.

Appellate participation by shareholder objectors is critical to ensuring that derivative settlements are in the best interests of the corporation. Appellate review provides an avenue for correcting errors and creates a powerful incentive for district courts to ensure that shareholder objections are given full and fair consideration during the settlement process. By contrast, a broad ruling that shareholder objectors must intervene to secure the right to appeal a derivative settlement would erect an unnecessary and costly barrier to shareholder participation and undermine the fairness and integrity of derivative settlements without providing any offsetting benefit.

[10] *See also Bolger*, 2 F.3d at 1310 (noting case where "objectors' ardent[] resistance to the settlement persuaded [the] court to look more closely at the proposal than would normally be the case" and caused the court to reject the proposal) (internal quotation marks omitted; alteration in original); *Seigal* v. *Merrick*, 619 F.2d 160, 162-63 (2d Cir. 1980) (highlighting role of objectors in modifying settlement by providing information regarding proper valuation method).

A. Appellate Review of Shareholders' Objections Is Essential to the Effective Monitoring of Derivative Suit Settlements.

The right to appeal an adverse judgment stands as "a fundamental element of procedural fairness as generally understood in this country." ABA Comm. on Standards of Judicial Admin., *Standards Relating to Appellate Courts* § 3.10 comment. at 18 (1994). Thus, although the right to an appeal is not mandated by the Constitution, "[i]t is almost axiomatic that every losing litigant in a one-judge court ought to have a right of appeal to a multijudge court." See Robert Leflar, *Internal Operating Procedures of Appellate Courts* 4 (1976) (Leflar, *Appellate Courts*). The principal function of intermediate appellate courts is the development of the law through the correction of error. See *id.* at 3 ("[T]he task of the appellate court is to determine if prejudicial errors were committed at the trial level and to correct them."). Indeed, the general rate of reversible error by district courts is significant, and, according to the most recent statistics, the federal courts of appeals remand or reverse in approximately 15% of non-prisoner, private civil appeals. See Administrative Office of the United States Courts, *Judicial Business of the United States Courts* 100-03, Table B-5 (1997).[11]

Apart from reversal, the possibility of appellate review itself provides a powerful incentive for the district court to render more careful findings of fact and to develop a better record, producing more accurate results in the district court *ex ante*. See Steven Shavell, *The Appeals Process as a Means of Error Correction*, 24 J. Legal Stud. 379, 408-11, 425-26 (1995)

[11] *See also* Jon O. Newman, *A Study of Appellate Reversals*, 58 Brook. L. Rev. 629, 633 (1992) (reporting rate of 27% in civil cases in the Second Circuit).

(demonstrating that the appeals process "induc[es] trial court judges to make fewer errors because of their fear of reversal"). Thus, direct review not only permits appellate courts to correct errors that have already occurred, it helps to prevent future errors from occurring, and thereby ensures uniform and proper application of the law. See Leflar, *Appellate Courts*, at 4 ("[G]rowth and development in the law cannot be achieved if some courts move ahead while others hold back.").

The important functions of appellate review apply with special force in the context of settlement of shareholder derivative actions. As described in Part I, shareholder derivative suits are fraught with the potential for collusion and conflicts of interest. Once a proposed settlement has been reached, the district court no longer has the benefit of an adversarial presentation by the parties regarding the benefits and burdens of the settlement proposal. And, laboring under an ever-expanding caseload, the district court may have a natural incentive to favor quick approval of a settlement that will remove a complex case from its docket at the expense of full and careful consideration of objections. These factors work together to enhance the risk of error by the district court in fairness hearings and to reduce the likely influence of shareholder objectors at the district court level. In light of these systemic obstacles to accurate assessment of proposed settlements, appellate review is critical to ensuring the fairness of shareholder derivative settlements.

For instance, in *In re Pittsburgh & Lake Erie R.R. Co. Sec. & Antitrust Litig.*, 543 F.2d 1058 (3d Cir. 1976), plaintiff stockholders sued on behalf of a company charging that a third party (which owned 93% of the stock) had raided the company's assets. *Id.* at 1061. Prior to trial, the parties reached a settlement providing that the company would pay $2.1 million into a settlement fund, which would have gone to

plaintiffs and their lawyers. *Id.* Irving Trust Company, an objector who was a pledgee of 22.5% of the company's stock, complained that the settlement was unfair because it would transfer value from the company to the plaintiffs and their attorneys. *Id.* at 1063. The district court rejected the objections and approved the settlement. *Id.* The Second Circuit reversed, holding that Irving Trust's objections should have been sustained because the settlement provided the company with, at best, "a minimal if non-existent benefit," in exchange for its substantial $2.1 million payment. *Id.* at 1070.[12]

The availability of appeal also causes trial courts to consider the objections of shareholders more carefully in the first instance. For example, in *Girsh* v. *Jepson*, 521 F.2d 153 (3d Cir. 1975), the Third Circuit reviewed a trial court's dismissal of objections interposed by a shareholder to a proposed compromise of a class and derivative action. *Id.* at 157. At the district court level, the shareholder informed the district court of her "intention to object" and asked for an extension of time "to file papers in support of her objections." *Id.* at 156. The district court dismissed her objections and approved the settlement agreement. *Id.* The Third Circuit reversed, holding that the "district court did not live up to its fiduciary responsibilities" because it denied the objecting shareholder "meaningful participation" in the hearing. *Id.* at 158. The *Girsh* Court also set forth the proper procedures district courts should follow when reviewing a proposed settlement. *Id.* at 156-57.

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[12] *See also Rosenbaum*, 64 F.3d at 1447 (reversing award of attorneys' fees based on arguments of non-intervening shareholder objector); *In re General Motors Corp. Pick-Up Truck Fuel Tank Prods. Liab. Litig.*, 55 F.3d 768, 809-10, 812-13 (3d Cir. 1995) (reversing class action settlement where the court was too dismissive of the objectors and too willing to accept the parties' optimistic valuation of the settlement).

Since *Girsh*, other district courts have followed the factors outlined in that case (including the requirement to consider the reaction of shareholders) to guide their assessment of proposed shareholder derivative settlements. See, *e.g.*, *In re Chambers Dev. Litig.*, 912 F. Supp. at 836 (stating that the factors enunciated in *Girsh* are the "Rand-McNally" of "settlement review"). Other circuit courts have adopted similar standards through appellate decisions that guide and bind their lower courts and ensure careful consideration of and a "reasoned response" to shareholder objections. *In re Pacific Enters. Sec. Litig.*, 47 F.3d at 377 (stating that "conclusory" rejection of an objection is inadequate because the district court must "explain[] why the derivative settlement is fair"). It is only through regular appellate review of derivative settlements that such beneficial rules can be articulated and refined, and compliance with them enforced.[13]

Thus, appellate review of derivative settlements serves to correct errors that have occurred and to guide the actions of trial courts and thereby reduce the chances that errors will occur in the first place.

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[13] *See also Ficalora* v. *Lockheed Cal. Co.*, 751 F.2d 995, 997 (9th Cir. 1985) (remanding for "reasoned judgment" that the settlement "is not the product of fraud or overreaching by, or collusion among, the negotiating parties"); *City of Detroit* v. *Grinnell Corp.*, 495 F.2d 448, 463 (2d Cir. 1974) (setting forth factors relevant to the review of a proposed settlement); *cf. Malchman* v. *Davis*, 706 F.2d 426, 432, 434 (2d Cir. 1983) (reversing approval of settlement because district court failed to consider objections fully); *In re General Motors Corp. Engine Interchange Litig.*, 594 F.2d 1106, 1131 (7th Cir. 1979) ("[W]e hold that the trial court abused its discretion by failing to undertake a careful examination of the conduct of the settlement negotiations and by preventing the plaintiff-objectors from showing that the negotiations prejudiced the best interests of the class.").

B. Requiring Intervention to Secure the Right to Appeal Would Cut Off Appellate Review of Some Derivative Settlements and Erect Unfair and Unnecessary Barriers to Effective Policing of Others.

Requiring objecting shareholders to intervene formally to secure the right to appeal the rejection of their objections to a proposed derivative settlement would prevent appellate review by some objectors and increase the costs for others. Moreover, while increasing the costs of objecting to derivative suit settlements, the added burden of intervention would produce no corresponding benefit to the litigation.

1. An Intervention Requirement Would Unduly Limit and Increase the Costs of Appeals by Shareholder Objectors.

In the decision below, the Seventh Circuit acknowledged that monitoring by shareholder investors "is often useful" and that objectors' participation on appeal may "be justified." Pet. Cert. 6a. However, the court of appeals concluded that such shareholder objectors "must intervene as parties in order to appeal from adverse decisions." *Id.* at 2a. That view should be rejected.

As an initial matter, requiring intervention would *prevent* an entire category of objections from being considered on appeal because some shareholder objectors could not, as a matter of law, intervene in the action. Specifically, the "contemporaneous ownership" rule requires the representative plaintiff in a shareholder derivative action to have been "a shareholder . . . at the time of the transaction of which the plaintiff complains." Fed. R. Civ. P. 23.1; see also *Rosenbaum* v. *MacAllister*, 64 F.3d 1439, 1443 n.2 (10th Cir. 1995). To

object to a proposed compromise, however, a person "need only own stock in the corporation at the time of the settlement hearing, and appear at the settlement hearing to raise his or her objections." *Id.*; see also Ralph C. Ferrara *et al.*, *Shareholder Derivative Litigation* § 14.04, at 14-10 (noting that "the ALI's *Principles of Corporate Governance* and other courts have suggested that all shareholders of record at the time of the settlement hearing have standing to object"). As a result, the entire category of objectors who obtained their stock *after* the transaction at issue in the case — shareholder objectors who have every bit as concrete and material an interest in the district court's resolution of the proposed settlement as shareholders who satisfy the contemporaneous ownership requirement — would "be held ineligible for intervenor status" and therefore could not raise any objections on appeal. *Rosenbaum*, 64 F.3d at 1443 n.2; see *Saylor* v. *Bastedo*, 78 F.R.D. 150, 152-53 (S.D.N.Y. 1978).

In addition, another class of objectors would be unable to intervene because their intervention would destroy diversity jurisdiction over their claims. See *Strawbridge* v. *Curtis*, 7 U.S. (3 Cranch) 267, 267 (1806) (requiring complete diversity). Federal law limits the ability of such non-diverse shareholder objectors to intervene in these cases. See 28 U.S.C. § 1367(b) (barring jurisdiction over non-diverse intervenors). As the Seventh Circuit recently noted, the plain language of § 1367(b) requires that "[p]laintiffs . . . intervening under Fed. R. Civ. P. 24 must satisfy the requirements of [complete diversity]." *Stromberg Metal Works* v. *Comfort Control, Inc.*, 77 F.3d 928, 932 (7th Cir. 1996) (Easterbrook, J.); see also *Turner/Ozanne* v. *Hyman/Power*, 111 F.3d 1312, 1319 (7th Cir. 1997) ("Section 1367 precludes intervention by parties seeking to 'intervene as plaintiffs under Rule 24 . . . when exercising supplemental jurisdiction over such claims would [destroy complete diversity].").

Moreover, even for shareholders who are diverse and have standing under Rule 23.1 to intervene as plaintiffs, the right to intervene would not be assured. In contrast to the mandatory requirements in Rule 23.1, which guarantee a shareholder objector the right to receive notice and to participate at the district court level, there is no comparable guarantee that a shareholder objector who first learns of a suit through notice of a proposed (and impending) settlement will be entitled to become a formal party. Indeed, a district court's grant of intervention would be predicated on its determination that the intervening parties' interests were not adequately protected, Fed. R. Civ. P. 24(a), a determination inconsistent with the requirement that the shareholder plaintiffs "adequately represent the interests of the shareholders" from the outset. Fed. R. Civ. P. 23.1; see also 7C Charles Alan Wright *et al.*, *Federal Practice & Procedure* § 1909, at 313. Further, Rule 24's requirement of a "timely application" prejudices would-be intervenors to a derivative suit, since Rule 23.1 requires notice only upon a settlement, which is so late in the litigation process that intervention is disfavored. See, *e.g.*, *Ragsdale* v. *Turnock*, 941 F.2d 501, 504 (7th Cir. 1991) ("Once parties have invested time and effort into settling a case it would be prejudicial to allow intervention."). Thus, it is not surprising that motions to intervene often are denied in shareholder derivative cases. See generally W.J. Dunn, *Intervention by Other Stockholders in Stockholder's Derivative Action*, 69 A.L.R.2d 562, at § 2a (1960).

Finally, the costs of intervention are substantial. To intervene, a motion and supporting papers must be prepared. See Fed. R. Civ. P. 24(c). Upon intervention, an objector must file a pleading based upon reasonable investigation stating the claims or defenses that he will advance, see *id.*, and provide initial discovery disclosures pursuant to Federal Rule of Civil Procedure 26(a)(1). Thereafter, the intervenor is subject to

broad discovery from both plaintiff and defendants. See Fed. R. Civ. P. 26(b). In particular, intervenors may be required to produce detailed information relating to their ability to represent the corporation adequately.

Given the risk of collusion and conflict of interest in shareholder derivative suits, these costs are likely to be greatest in those cases where the right to appeal is most important.[14] Because shareholder objectors pose a threat to potentially unfair and collusive settlements, the parties to these suits have a strong incentive to obstruct any vigorous objection to the settlement at both the district court and appellate levels.

Indeed, the additional costs associated with intervention stand in marked contrast to the efficient procedures expressly mandated by Rule 23.1, which permit shareholders to air their objections in court *without* assuming the burdens associated with formal intervention. See Fed. R. Civ. P. 23.1. The drafters of Rule 23.1 plainly intended to entitle shareholders to present their concerns regarding a proposed settlement to the district court, free from strategic behavior or sharp litigation tactics designed to increase the cost of objection. It was precisely to avoid the risks associated with imposing additional obstacles to challenging proposed derivative settlements that the Third Circuit ruled that intervention was not required to ensure appellate rights on appeal. See *Bolger*, 2 F.3d at 1310.

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[14] Even small increases in costs imposed on the monitoring function will have a substantial effect on the incentive and ability of shareholders to restrain unfair settlements. Plaintiffs and their attorneys typically have a large stake in the settlement and can afford to litigate aggressively. By contrast, because of collective action problems endemic to derivative suits, *Bolger*, 2 F.3d at 1310, objectors act to protect only their own individual interests. Therefore, it takes only a marginal increase in litigating costs to dissuade potential objectors from participating. *Cf. id.* at 1309 ("[T]he costs of policing typically outweigh any pro rata benefits to the shareholder.")

Evidence from a related context confirms the operation of the incentives described above. Responding to similar abuses inherent in securities class actions, Congress passed the Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, 109 Stat. 737 (1995), which had as one of its purposes the goal of increasing the role of institutional investors as lead plaintiffs in class actions. See H. Conf. Rep. No. 369, 104th Cong., 1st Sess. 34 (1995), *reprinted in* 1995 U.S.C.C.A.N. 730, 733 ("Institutional investors and other class members with large amounts at stake will represent the interests of the plaintiff class more effectively than class members with small amounts at stake."). Faced with the threat of institutional investor participation, the plaintiffs' bar responded by attempting to drive up the litigation costs for institutional investors. As a result of these efforts, "[i]nstitutional investors are only rarely stepping forward to become lead plaintiffs. They are often vigorously attacked by traditional plaintiffs' counsel when they do." Joseph A. Grundfest & Michael A. Perino, *Joint Written Testimony Before the Subcommittee on Securities of the Senate Committee on Banking, Housing, and Urban Affairs* (July 24, 1997); see also *Gluck* v. *Cellstar Corp.*, 976 F. Supp. 542, 547-48 (N.D. Tex. 1997) (detailing one such struggle).

As a final note, even if respondents were correct in their suggestion that intervention would be "unhesitatingly granted" for the limited purpose of appeal, Resp. Opp. to Cert. 16, that fact would counsel against imposing an additional intervention requirement. Put simply, if every objecting shareholder were permitted to intervene to secure the right to advance his objections on appeal, then the intervention process would be an empty formality that imposes additional costs but provides no benefits to the district court or court of appeals.

2. An Intervention Requirement Would Provide No Corresponding Benefit.

The substantial costs of intervention would create an additional barrier to effective shareholder policing of derivative settlements without any corresponding benefit, either to the efficiency or to the fairness of the litigation process.

First, an intervention requirement would add nothing to the character or substance of the appeals brought by objecting shareholders. As owners of the corporation, shareholder objectors suffer a concrete injury when an unfair settlement diminishes the value of their investment; indeed, Rule 23.1 expressly solicits the views of these shareholders as a means of policing the potential abuses endemic to shareholder derivative litigation. The challenges they raise on appeal would be the same challenges raised and rejected by the district court. See *Bolger*, 2 F.3d at 1310 (holding that participation as an objector before the trial court is sufficient to permit "the same objections he now raises . . . on appeal"). There is simply no basis for concluding that shareholder objectors, who are recognized as adding value to the analysis of a settlement proposal at the district court level, are not equally well-positioned to provide guidance and insight at the appellate level.

Second, historical experience makes clear that the imposition of an intervention requirement will provide little or no benefit to appellate courts. For many years, numerous state courts and federal circuit courts have routinely allowed shareholder objectors to appeal adverse rulings without any intervention requirement. See, *e.g.*, *Rosenbaum* v. *MacAllister*, 64 F.3d 1439, 1443 (10th Cir. 1995); *Bolger*, 2 F.3d at 1307-10; *In re General Tire & Rubber Co. Sec. Litig.*, 726 F.2d 1075, 1087 (6th Cir. 1984) (affirming denial of intervention but addressing shareholder's objections on appeal); *In re Pittsburgh*

& Lake Erie R.R. Co. Sec. & Antitrust Litig., 543 F.2d 1058, 1064 (3d Cir. 1976) (holding that objector has standing to appeal); *Tryforos* v. *Icarian Dev. Co.*, 518 F.2d 1258, 1263 n.22 (7th Cir. 1975) (Stevens, J.) (stating that the "law is clear" that non-party objectors may appeal); *Braun* v. *Fleming-Hall Tobacco Co.*, 92 A.2d 302, 308 (Del. Ch. 1952) (reviewing appeal of non-intervening objector). There is no evidence in these jurisdictions of a proliferation of meritless appeals or "unwieldy" appellate litigation of settlement objections. Indeed, requiring intervention would create an extra layer of largely wasteful appeals from the denial of intervention.

Third, cases from other contexts have acknowledged the appellate rights of non-parties whose interests have been concretely and adversely affected by the decision of the district court. There is a long pedigree of cases that "clearly establish that nonparties can achieve standing to appeal." 15A Charles Alan Wright *et al.*, *Federal Practice & Procedure* § 3902.1 at 132; see also Timothy A. Duffy, Comment, *The Appealability of Class Action Settlements by Unnamed Parties*, 60 U. Chi. L. Rev. 933, 940-41 (1993) (describing deep-rooted common-law origins of right of unnamed class members to appeal). The readiest example is that of an appellant, not a party, who has nevertheless been enjoined, held in contempt, or otherwise directly affected by an order of the district court. See, *e.g.*, *United States Catholic Conference* v. *Abortion Rights Mobilization, Inc.*, 487 U.S. 72, 76 (1988) ("The right of a nonparty to appeal an adjudication of contempt cannot be questioned."); *Thompson* v. *Freeman*, 648 F.2d 1144, 1447 n.5 (8th Cir. 1981) (holding that non-party may bring "appeal to contest the district court's jurisdiction to bind it to the terms of the court's injunction"). Similarly, when a party is denied statutory attorney fees by the district court, that party's attorney has standing to appeal. See, *e.g.*, *Lipscomb* v. *Wise*, 643 F.2d 319, 320 (5th Cir. 1981); *Dietrich Corp.* v. *King Resources*

Co., 596 F.2d 422, 424 (10th Cir. 1979). In *Dietrich*, the court noted that intervention was irrelevant to appellate rights; the controlling factor was that denying the attorney the right to appeal would render the district court's determination unreviewable. See *id.* In *Lipscomb*, the fees were sought pursuant to 42 U.S.C. § 1973*l*(e), and the court of appeals concluded that if the statutory provision of fees were to have any meaning, the non-party whose interest was implicated must be able to seek appellate review. *Lipscomb*, 643 F.2d at 320-21.

The same is true here: If objecting non-party shareholders are not entitled to appeal after their objections lodged under Rule 23.1 have been rejected, then the concrete and important interests they represent will never receive an appellate hearing. The consequence of such a requirement would be more collusive and unfair derivative settlements. As Congress and the drafters of the Federal Rules of Civil Procedure were plainly of the view that objecting shareholders could make valuable contributions to district court review of such settlements, there is no sound reason in law or policy to bar or discourage them from playing a similar role on appeal.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted,

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In the Supreme Court of the United States

OCTOBER TERM, 1998

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM AND FLORIDA STATE BOARD OF ADMINISTRATION,
Petitioners,

v.

PAUL FELZEN, ET AL.,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

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BRIEF FOR BARCLAYS GLOBAL INVESTORS, N.A., STATE OF WISCONSIN INVESTMENT BOARD, AND CERTAIN OTHER INSTITUTIONAL INVESTORS AS AMICI CURIAE SUPPORTING PETITIONERS

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36pp

TABLE OF CONTENTS

Page

INTEREST OF THE AMICI CURIAE 2

SUMMARY OF ARGUMENT 4

ARGUMENT 6

I. REQUIRING INTERVENTION BEFORE APPEAL WOULD PREVENT MERITORIOUS APPEALS BY DENYING MANY INSTITUTIONAL INVESTORS THEIR ABILITY TO APPEAL 6

A. Because of the differences between intervention and objection, institutional investors cannot, as a practical matter, make timely intervention decisions in all cases in which an appeal might be warranted 7

1. A decision to object or appeal is substantially different from a decision to intervene 7

2. Practical constraints on institutional investors prevent them from making timely intervention decisions in all cases in which an appeal might be warranted 10

B. The need for complete diversity of citizenship would frequently prevent objecting shareholders from intervening 15

C. Denying appeals by institutional investors would prevent meritorious appeals 17

D. Requiring a limited form of intervention for purposes of appeal would not fully address the concerns of institutional investors 20

II. FEDERALISM AND *ERIE* CONSIDERATIONS FAVOR PERMITTING SHAREHOLDERS TO APPEAL WITHOUT INTERVENING 22

CONCLUSION 27

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CASES

Amchem Products, Inc. v. Windsor,
521 U.S. 591, 117 S. Ct. 2231 (1997) 19, 21

Auerbach v. Bennett,
393 N.E.2d 994 (N.Y. 1979) 25

Barney v. Hubbard,
No. 692583 (Super. Ct., San Diego County, Cal. 1996) 11

Bell Atlantic Corp. v. Bolger,
2 F.3d 1304 (3d Cir. 1993) 10

California, Rebney v. Wells Fargo Bank, N.A.,
269 Cal. Rptr. 844 (Ct. App. 1990) 25

Central Wesleyan College v. W.R. Grace & Co.,
6 F.3d 177 (4th Cir. 1993) 16

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337 U.S. 541 (1949) 23,24

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127 F.2d 721 (6th Cir. 1942) 18

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54 F.3d 156 (3d Cir. 1995) 16

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304 U.S. 64 (1938) 22

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518 U.S. 415 (1996) 22,26

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(6th Cir. 1992) 16

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380 U.S. 460 (1965) 22, 23

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543 F.2d 1058 (3d Cir. 1976) 18

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500 U.S. 90 (1991) 24

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313 U.S. 487 (1941) 22

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996 F.2d 928 (7th Cir. 1993) 16

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168 F.R.D. 90 (D. Me. 1996) 16

Posen v. Cowdin,
44 N.Y.S.2d 842 (App. Div. 1943) 25

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636 A.2d 915 (Del. 1994) 24

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714 So. 2d 1146 (Fla. Dist. Ct. App. 1998) 25

Rosenbaum v. MacAllister,
64 F.3d 1439 (10th Cir. 1995) 7, 18

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394 U.S. 332 (1969) 16

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487 U.S. 22 (1988) 22

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271 U.S. 176 (1926) 21

Trotsky v. Los Angeles Federal Savings & Loan Assoc.,
121 Cal. Rptr. 637 (Ct. App. 1975) 25

Walker v. Armco Steel Corp.,
446 U.S. 740 (1980) 22,23

STATUTES & RULES

15 U.S.C. § 78u-4(a)(3)(A) 11

28 U.S.C. § 1332 16

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Fed. R. Civ. P. 23 19

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BRIEF FOR BARCLAYS GLOBAL INVESTORS, N.A., STATE OF WISCONSIN INVESTMENT BOARD, AND CERTAIN OTHER INSTITUTIONAL INVESTORS AS AMICI CURIAE SUPPORTING PETITIONERS

The institutional investors listed in the Appendix ("Institutional Investors") respectfully submit this brief as amici curiae supporting the petitioners, California Public Employees' Retirement System and Florida State Board of Administration.[1] The Institutional Investors believe that the

[1] The parties consented to the filing of this brief. Their letters of consent are on file with the Clerk of the Court.

Counsel for a party did not write any part of this brief. The (continued...)

Seventh Circuit's rule requiring a shareholder that plans to object to the terms of settlement in a derivative case to intervene to preserve its ability to appeal imposes unnecessary and undue costs and will deter meritorious appeals. They therefore request the Court to reverse the Seventh Circuit and permit the Petitioners to appeal the settlement of the derivative case without intervening.

INTEREST OF THE AMICI CURIAE

Each of the Institutional Investors listed in the Appendix has a significant interest in the resolution of this case. The Institutional Investors have sizable securities holdings in a large number of U.S. corporations and are often among the securities owners represented by the named shareholders in shareholder derivative actions. They therefore favor legal rules permitting them to improve the terms of derivative case settlements without encountering unnecessary costs and procedural hurdles.

Each Institutional Investor is a large private or public investment fund or the investment manager for such a fund with tens of billions of dollars under management. The amici along with other institutional investors[2] "are America's largest shareholders, with about $9.5 trillion in assets,

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[1] (...continued)
Council of Institutional Investors, which is an association of institutional investors, made a monetary contribution to the preparation and filing of this brief.

[2] Institutional investors take many forms, such as banks, mutual funds, and private and public pension funds. See Margaret Blair, Ownership and Control 147-65 (1995); Robert A. G. Monks & Nell Minow, Corporate Governance 120-45 (1995).

accounting for fifty-one percent of the equity market."[3] Of the Institutional Investors, Barclays Global Investors, N.A. manages, administers, or advises on the investment of over $500 billion in assets. The New York State Common Retirement Fund has assets with a value of approximately $105 billion. The New York City pension funds have assets of over $84 billion, and the New York State Teachers' Retirement System has approximately $70 billion.

At any one time, each Institutional Investor generally owns or manages the securities of hundreds or thousands of issuers, roughly half or more of which are U.S. corporations. For example, Barclays Global has approximately $320 billion of its $500 billion in assets under management invested in U.S. securities, mostly equities. The New York City funds own approximately $50 billion of U.S. equities out of total holdings of $84 billion. The New York State Common Retirement Fund has approximately $52 billion invested in the common stock of more than 1,600 different U.S. issuers.

A fund's stake in the common stock of a U.S. company ranges from a small fraction of one percent to over 17 percent. The State of Wisconsin Investment Board ("SWIB") owns more than 10 percent of 35 companies. The investment of the New York State Common Retirement Fund in a single issuer ranges from a few thousand dollars to over $1 billion.

The Institutional Investors manage their holdings on behalf of millions of individual beneficiaries. The New York City pension systems have more than 540,000

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[3] H.R. Conf. Rep. No. 104-369, at 34 (1995), reprinted in 1995 U.S.C.C.A.N. 730, 733.

participants, including beneficiaries, retirees, vested members, and active members. SWIB has over 435,000 participants, who are state, university, public school, and local government employees. The New York State Common Retirement Fund has approximately 867,000 members and beneficiaries.

The objective of the Institutional Investors is to maximize the long-term return on their securities investments for the benefit of all their individual participants, and they do that by, among other things, monitoring and exercising their shareholder authority over the boards of directors and managers of corporations in which the funds invest. Derivative actions are one of the important methods shareholders use to hold directors and officers accountable for the conduct of corporate affairs. Given that the great majority of derivative actions are settled rather than litigated, the Institutional Investors therefore have a substantial interest in a resolution of this case that enhances their opportunities to affect the terms on which derivative cases are settled.

SUMMARY OF ARGUMENT

The Court should reverse the ruling of the Seventh Circuit in this case because requiring an objecting shareholder to intervene to preserve its ability to appeal a district court approval of a derivative settlement would prevent meritorious appeals. Because a decision to intervene has significantly greater costs and legal consequences than a decision to object or appeal, a variety of practical constraints on institutional investors would prevent them from making timely intervention decisions in all cases in which an appeal might be needed. These practical constraints include inadequate time to consider proposed settlement terms, lengthier procedures for making decisions to intervene, and

limited resources for coping with the larger responsibilities associated with intervention. In addition, in derivative cases in federal court based on diversity of jurisdiction, many shareholders would probably not be able to intervene because doing so would destroy complete diversity. As a result, an intervention requirement would effectively deny many institutional investors their ability to appeal.

Denying institutional investors an opportunity to appeal would harm the judicial process because the number of inadequate and unfair settlements would increase. Appeals by objecting, non-intervening shareholders have in the past successfully challenged derivative settlements approved by district courts, and the loss of the threat of appeal would diminish a shareholder's ability to improve settlement terms at the district court level.

Federalism and *Erie* considerations also favor permitting shareholders to appeal without intervening. States have a strong interest in preventing unfair and inadequate settlements of derivative cases based on state law claims, and several states that are preferred locations for incorporation and shareholder derivative cases do not require an objecting shareholder to intervene before appealing. The Court should take this state practice into account in determining whether an objecting shareholder in federal court must intervene to appeal.

ARGUMENT

I. REQUIRING INTERVENTION BEFORE APPEAL WOULD PREVENT MERITORIOUS APPEALS BY DENYING MANY INSTITUTIONAL INVESTORS THEIR ABILITY TO APPEAL.

The Institutional Investors strongly believe that, because of differences between a decision to intervene and a decision to object or appeal, requiring an objecting shareholder to intervene to preserve its ability to appeal a district court approval of a derivative settlement would prevent meritorious appeals. An intervention requirement would prevent appeals because intervention imposes unnecessary costs in the circumstances of a settlement challenge and because a variety of practical constraints on institutional investors would prevent them from making a timely decision to intervene in all cases in which they might decide that an appeal is warranted. In addition, in derivative cases in federal court based on diversity of jurisdiction, many shareholders would probably not be able to intervene because doing so would destroy complete diversity.

In the next sections of the brief, we address these issues. We then explain that discouraging appeals by institutional investors will harm the judicial system and finally discuss why requiring only a limited form of intervention for purposes of appeal would not fully address the concerns of the Institutional Investors.

A. Because of the differences between intervention and objection, institutional investors cannot, as a practical matter, make timely intervention decisions in all cases in which an appeal might be warranted.

1. A decision to object or appeal is substantially different from a decision to intervene.

A decision to object to a settlement or appeal the approval of a settlement of a derivative case is substantially different from a decision to intervene. An objector or an appellant generally has a narrow and specific disagreement or set of disagreements with a proposed settlement. For example, the shareholder might believe that the proposed payment of legal fees is too high[4] or that the money damages payable to the corporation are too low. As in this case, the objector might challenge the adequacy or effectiveness of the proposed changes in the structure of the board of directors or in the system of corporate governance.

An objector, taking into account the uncertainties of proceeding to trial, seeks to ensure that the terms of the settlement adequately compensate the corporation for the alleged misconduct and harm to the corporation. An objector's goal is not to control the prosecution of the case and establish the liability of the defendants.

A decision to intervene has broader purposes and more significant legal consequences. For several reasons, an intervening shareholder assumes more responsibility and

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[4] See, e.g., Rosenbaum v. MacAllister, 64 F.3d 1439 (10th Cir. 1995) (in combined class and derivative action, objector challenged only attorney fee award and not settlement agreement as a whole).

faces a considerably greater commitment of time, energy, and resources than an objecting shareholder.

First, to comply with Rule 24 of the Federal Rules of Civil Procedure, an intervenor must file a motion to intervene and must include a pleading setting forth the claim or defense for which intervention is sought. Before filing the pleading, the intervenor must conduct sufficient due diligence to satisfy the requirements of Rule 11. If the motion is opposed, the intervenor must reply and, if the motion is denied, appeal.

Second, a successful intervenor has party status.[5] A shareholder intervening in a derivative case becomes one of the plaintiffs pursuing the best interests of all the shareholders and of the corporation[6] and making all the decisions a client in litigation makes. It has responsibilities for prosecuting the case, for collecting evidence, for establishing the liability of the defendants, and for obtaining the best possible relief by settlement or judgment.

Third, an intervenor bears all the burdens of a party. It becomes subject to all discovery provisions applicable to a party, such as the obligation to make initial disclosures and answer interrogatories. The other parties may obtain documents and depositions from an intervenor much more easily than from a person not a party.

These differences between intervening and objecting to a settlement and perhaps appealing the trial court's approval of the settlement materially affect a shareholder's cost-benefit

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[5] 7C Charles Alan Wright et al., Federal Practice and Procedure § 1920 (2d ed. 1986).

[6] See Smith v. Ayres, 977 F.2d 946, 949 (5th Cir. 1992).

analysis when deciding whether to take a position in a particular case. For each case, a shareholder must evaluate whether the benefits it will receive either in the particular case or across its portfolio are likely to exceed the costs, including lost opportunities, to it or its beneficiaries of taking action, subject to the chance of being reimbursed some or all of its legal fees and costs.

Requiring intervention would disproportionately increase the costs and stakes when compared with the objective or the potential benefit. A shareholder with an objection to the terms of a proposed settlement has a limited and particular goal accompanied by discrete and manageable costs, even taking into account the possibility of an appeal. Intervention on the other hand dramatically increases the shareholder's responsibilities and cost exposure with little or no corresponding benefit. An institutional investor would need to consider whether assuming these broad obligations of an intervenor would be consistent with its fiduciary duties to its beneficiaries, an issue that does not arise in connection with an objection or appeal. These additional and disproportionate costs would discourage intervention.[7]

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[7] See Elliott J. Weiss & John S. Beckerman, Let the Money Do the Monitoring: How Institutional Investors Can Reduce Agency Costs in Securities Class Actions, 104 Yale L.J. 2053, 2095-103 (1995) (describing procedures in class actions that deter institutional investors from acting as named plaintiffs); see also note 15 and accompanying text below.

2. Practical constraints on institutional investors prevent them from making timely intervention decisions in all cases in which an appeal might be warranted.

For a variety of practical reasons related to the way that institutional investors and shareholder derivative cases actually operate, the differences between intervention and objection or appeal mean that an intervention requirement would effectively deny many institutional investors their ability to appeal. Institutional investors typically receive inadequate notice of proposed settlements, have lengthy procedures for making decisions as important as intervention, and have limited budgets and personnel to devote to shareholder litigation.

Short notice. Most of the Institutional Investors typically own the securities of over 1000 U.S. corporations. Monitoring costs prevent them from learning of every derivative case filed in federal court on behalf of a corporation in which they own securities. As a result, institutional investors often learn of a derivative case and the proposed settlement at the same time, when the notice of the settlement arrives in the mail.[8] Even when a shareholder is generally aware that a derivative case is pending, it usually does not learn of the specific terms of a proposed settlement

[8] See Bell Atlantic Corp. v. Bolger, 2 F.3d 1304, 1309 n.9 (3d Cir. 1993); Weiss & Beckerman, supra note 7, at 2100-01; Jonathan R. Macey & Geoffrey P. Miller, The Plaintiffs' Attorney's Role in Class Action and Derivative Litigation: Economic Analysis and Recommendations for Reform, 58 U. Chi. L. Rev. 1, 20 (1991).

Other types of cases now involve a requirement for earlier notice. Since 1995, a plaintiff in a class action alleging a violation of the federal securities laws must publish a notice about the pendency of the case. See, e.g., 15 U.S.C. § 78u-4(a)(3)(A).

until it receives formal notice.

In this case, for example, shareholders had less than five weeks to react to the terms of the proposed settlement. The district court entered an order on May 30, 1997 providing for notice to shareholders of the settlement and requiring written objections by July 3, 1997.

Occasionally, the notice is even shorter. SWIB, one of the amici Institutional Investors, regularly receives notice a week or less before a settlement hearing and, in one derivative case,[9] received no formal notice, learning informally from another shareholder that objections to a settlement were due in two days.

These short notice periods mean that an institutional investor has only a limited amount of time to assess the case and the proposed settlement and decide on a course of action. Formulating objections in these time periods is difficult, but, as we now describe, reaching a decision to intervene requires even more time.

Long decision-making processes. Because of the significant legal and financial consequences of intervention discussed above, most institutional investors have lengthy procedures for making a decision to intervene or become a party. The procedure usually takes several months and can take much longer. Generally, although the internal procedures of the Institutional Investors differ, they do not need to obtain the same level of approval or follow the same lengthy decision-making process to file an objection to a proposed derivative settlement or to appeal a settlement

[9] Barney v. Hubbard, No. 692583 (Super. Ct., San Diego County, Cal. 1996).

approval as they do in deciding to intervene as a party.

The typical procedure is for a staff lawyer or outside counsel retained specifically for the matter to evaluate the case and prepare an analysis and recommendation that considers the likelihood of success, the likely recovery, and the probable costs of intervening or objecting.[10] If the senior staff approves the recommendation, the board of nearly all the Institutional Investors must also approve. Boards generally meet only monthly or quarterly, and items to be discussed usually must be on the agenda well in advance. Although many boards have emergency meeting procedures, they are generally not intended to be used for litigation matters. After the board decides to proceed, further approvals, such as from the state attorney general or the city attorney, are sometimes needed. At many of the Institutional Investors, the entire process to reach a decision to intervene would take three to four months.

Several factors account for this careful deliberative process. The process reflects the fiduciary duties institutional investors owe to their beneficiaries under the Employee Retirement Income Security Act or comparable federal or state statutes.[11] In derivative cases, when the recovery goes to the corporation and benefits all shareholders, the probable costs of intervention nearly always exceed the likely benefits to the particular fund,

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[10] Weiss & Beckerman, supra note 7, at 2117.

[11] See Blair, supra note 2, at 156-64; Weiss & Beckerman, supra note 7, at 2112-20; Amendments to Beneficial Ownership Reporting Requirements, Exchange Act Release No. 34-39538, 66 SEC Docket (CCH) 596, 601 (Jan. 12, 1998) ("The Commission believes that these plans [public pension plans] are now generally subject to fiduciary obligations and standards for investment that are substantially similar to those imposed by [Employment Retirement Income Security Act].").

unless the investor receives beneficial broader portfolio effects from the action. Fund managers therefore must select wisely and choose to participate only in those cases offering the potential for setting a useful precedent or deterring similar misconduct in other companies.[12] The lengthy deliberative process also reflects that many of the boards are public bodies subject to administrative law requirements[13] and have many members with diverse perspectives and different interests.

Limited resources. Most institutional investors have extremely limited resources, in part as a result of the need to keep the costs of investment services down or to comply with statutory obligations requiring administrative expenses to be kept at a reasonable level. Adding an intervention requirement would strain these limited resources and tax the ability of institutional investors to react to notices of proposed settlements, prepare careful evaluations for their boards about the implications of intervention, and make the commitment required of an intervenor.

Many institutional investors, especially public pension funds, have small legal budgets and small legal staffs. Even large public funds generally employ no more than five or six lawyers and a few paralegals to handle all of the legal work of the fund, including investor issues, real estate transactions, and disputes with beneficiaries. The annual

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[12] See generally Keith L. Johnson, Deterrence of Corporate Fraud Through Securities Litigation: The Role of Institutional Investors, 60 L. & Contemp. Prob. 155, 159 (1997); Bernard S. Black, Agents Watching Agents: The Promise of Institutional Investor Voice, 39 UCLA L. Rev. 811, 834-35, 839 (1992).

[13] See, e.g., Cal. Education Code §§ 22350-62 (West 1994 & Supp. 1998) (guidelines governing investment of funds in the California State Teachers' Retirement System).

legal budgets of the Institutional Investors vary depending on several factors, such as the nature of the investments, but generally are lean. The budget at many institutional investors for inside and outside lawyers for all matters ranges from approximately $150,000 to $500,000, although some have substantially larger amounts. Public funds often need legislative approval for budget increases or special appropriations.

These limitations are practical constraints on institutional investors inclined to object or appeal, but they take on much greater significance when an institutional investor considers intervention because of the larger consequences of intervention. The limited resources restrict the efforts of institutional investors to monitor shareholder litigation, react to proposed settlements, prepare intervention recommendations for their boards, and then prepare the papers and muster the resources, such as litigation lawyers, to intervene.

The limited resources also restrict the ability of institutional investors to intervene because the increased responsibilities of intervening require more money and staff time than objecting or appealing. Responding to broad and potentially abusive discovery requests[14] distracts investment staff from their normal functions and can result in the loss of profitable trading opportunities. Supervising the lawyers representing the intervenor also involves a substantial commitment of time and attention.

The Assistant General Counsel of SWIB recently summarized the risks and costs that institutional investors perceive as disincentives to becoming plaintiffs in securities

[14] See Weiss & Beckerman, supra note 7, at 2102-03.

class actions:

> Their concerns include costs associated with exposure to discovery, time needed to manage the litigation, possible public disclosure of proprietary investment information, and fear that other plaintiffs who disagree with how the case was handled might sue them.[15]

These same factors would cause institutional investors to proceed with greater care when considering whether to intervene in a derivative case.

In sum, the greater burdens and costs associated with intervention, the need to follow long, careful decision-making procedures before becoming a party, the diversion of limited resources, and other costs create practical obstacles to the ability of institutional investors to intervene in a timely way in shareholder derivative cases. The relatively small number of institutional investors that have become lead plaintiffs under the terms of the Private Securities Litigation Reform Act evidence these problems.[16]

B. The need for complete diversity of citizenship would frequently prevent objecting shareholders from intervening.

Because a shareholder intervening in a derivative action has the status of a party plaintiff, it must have an

[15] Johnson, supra note 12, at 159 (1997) (citing Office of the General Counsel, Securities and Exchange Commission, Report to the President and Congress on the First Year of Practice Under the Private Securities Litigation Reform Act of 1995, at 51 (1997)).

[16] See Johnson, supra note 12, at 159.

independent basis for federal court jurisdiction.[17] In derivative cases, the usual basis is diversity of citizenship because the claims are commonly allegations of breach of fiduciary duty by officers or directors in violation of state law. If the citizenship of the proposed intervenor would eliminate complete diversity, a substantial risk exists that, since the 1990 adoption of the supplemental jurisdiction statute, the district court would deny intervention.[18] At a minimum, the shareholder would face uncertainty and increased costs of litigation in connection with the proposed intervention, each of which would deter participation.

As a result, the rule of the Seventh Circuit obstructs the

[17] 6 James W. Moore et al., Moore's Federal Practice § 24.22[1]-[2] (3d ed. 1997); 7C Wright et al., supra note 5, § 1917.

[18] See 28 U.S.C. § 1332; Snyder v. Harris, 394 U.S. 332, 340 (1969) (the citizenship of the named plaintiffs in a class action must be diverse from the citizenship of the defendants); Central Wesleyan College v. W.R. Grace & Co., 6 F.3d 177, 186 n.3 (4th Cir. 1993) (same); 28 U.S.C. § 1367 (in a diversity case, a court shall not have supplemental jurisdiction over claims by persons "seeking to intervene as plaintiffs under Rule 24 ... when exercising such jurisdiction would be inconsistent with the jurisdictional requirements of section 1332."); Development Fin. Corp. v. Alpha Housing & Health Care, Inc., 54 F.3d 156, 159 (3d Cir. 1995); Krueger v. Cartwright, 996 F.2d 928, 933 n.6 (7th Cir. 1993); Liberty Mutual Group v. Hillman's Sheet Metal, 168 F.R.D. 90, 92 (D. Me. 1996) ("[T]he weight of authority supports the conclusion that § 1367(b) precludes the exercise of supplemental jurisdiction over claims by nondiverse plaintiff-intervenors, even as of right under Rule 24(a)."). But see Costain Coal Holdings, Inc. v. Resource Investment Corp., 15 F.3d 733 (7th Cir. 1994) (reasserting rule that diversity is destroyed only if the nondiverse intervenor was indispensable at the time the complaint was filed); Grossheim v. Freightliner Corp., 974 F.2d 745 (6th Cir. 1992) (intervention of nondiverse silent party plaintiff did not destroy diversity jurisdiction because intervenor was not an indispensable party when litigation commenced).

ability of many objecting shareholders to appeal when a derivative case is based on diversity of citizenship and the citizenship of the objector is the same as any defendant. Either trial courts would deny intervention to preserve complete diversity or shareholders would not seek to intervene because of the costs of litigating the issues over intervention. Without intervening, the shareholder could not appeal, and its objections, if filed at all, would carry reduced weight with the parties and the court. Accordingly, the Court should not impose an intervention requirement unless it also determines that intervention by a plaintiff with the same citizenship as a defendant does not destroy diversity.

C. Denying appeals by institutional investors would prevent meritorious appeals.

Because imposing an intervention requirement would prevent institutional investors as a practical matter from appealing or threatening to appeal derivative settlements, the number of inadequate settlements would increase, and that would significantly undermine the fairness of, and respect for, the judicial process. History shows that appeals by non-intervening shareholder objectors will in some cases be all that prevents an unfair settlement from receiving final judicial approval. Even if there is some slight benefit to be derived from the intervention requirement imposed by the court below -- which the Institutional Investors contest -- it would be dwarfed by the harm flowing from the reduced ability of the federal appellate courts to assure that the judicial imprimatur is not placed on unjust derivative settlements.

The efficacy of the current judicial process for assuring the adequacy and fairness of derivative and class settlements

has already been criticized.[19] The troubling shortcomings of this system flow from the acknowledged problem that frequently none of the settling parties has an incentive to assure that all material information relating to the fairness determination is brought to the attention of the trial or appellate court.[20] Sometimes justice prevails only because a non-intervening objector was able to challenge a settlement on appeal.[21]

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[19] In a study of shareholder suits from the late 1960s through 1987, approximately two-thirds of the derivative suits settled, and the settlements typically produced at best negligible monetary payouts and essentially cosmetic structural relief. Roberta Romano, The Shareholder Suit: Litigation Without Foundation?, 7 J.L. Econ. & Org. 55, 70, 84 (1991). See generally 2 ALI, Principles of Corporate Governance: Analysis and Recommendations 4-16, 183-96 (1994).

[20] This problem often occurs because the derivative plaintiff's counsel, not the plaintiff itself, has the most at stake:

> In the context of shareholder derivative suits and class actions that concern publicly held corporations, it is in reality usually the lawyer rather than the client who makes the important litigation decision about whether to settle and for how much. The actual shareholder client often has, at best, a nominal economic stake in the outcome of the litigation. Therefore, shareholders often lack sufficient economic interest to pay the information costs and expend the energy required to keep abreast of the progress of the litigation and to make informed decisions. . . . This conflict of interest may lead lawyers in derivative suits or class actions to enter into settlement agreements with the defendant directors and officers before the suits reach trial, even though they might have had a realistic chance of obtaining favorable judgments for their clients.

Tim Oliver Brandi, The Strike Suit: A Common Problem of the Derivative Suit and the Shareholder Class Action, 98 Dick. L. Rev. 355, 389 (1994) (footnotes omitted).

[21] See, e.g., Rosenbaum v. MacAllister, 64 F.3d 1439 (10th Cir.

(continued...)

A recent example of the importance of non-intervenor appeals in class and derivative actions is this Court's ruling in *Amchem Products, Inc. v. Windsor*,[22] a case the Court selected to clarify class certification standards in settlements. *Amchem* involved a settlement approved by the district court and overturned in an appeal the Third Circuit allowed by non-party class members that had not been permitted to intervene. This Court ruled that the district court, in an understandable desire to approve the settlement of a complex array of cases, glided too easily past certain requirements of Rule 23, including important considerations relating to intra-class conflicts of interest. The guidance for future cases provided by *Amchem*, and the increased fairness of the settlement process for the asbestos claims in that case, were the direct result of an appeal by non-intervenor objectors.

Imposing a formal intervention requirement would make the problems with derivative case settlements more acute. The costs of participation would increase, closing the doors of the appellate courts to institutional investors in many cases

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[21] (...continued)

1995) (non-intervenor appellant successful in challenging excess attorney's fees in settlement of class and derivative action); In re Pittsburgh & Lake Erie R.R. Co. Sec. & Antitrust Litig., 543 F.2d 1058 (3d Cir. 1976) (settlement involving payments to attorneys and minority shareholder overturned on appeal by non-intervening objector because detriment to the corporation far outweighed any benefits it received); Cohen v. Young, 127 F.2d 721 (6th Cir. 1942) (derivative settlement approved on the basis of purported insolvency of defendant overturned on appeal because lower court failed to undertake an informed assessment of the supposed insolvency).

Another lesson of the cases is that frivolous or meritless appeals have not been a problem. In any event, to the extent that problem does occur, other sanctions, such as Rule 38 of the Federal Rules of Appellate Procedure, are available and adequate.

[22] 521 U.S. 591, 117 S. Ct. 2231 (1997).

and preventing appellate review of some inadequate and collusive settlements. Because of the absence of the threat of appeal, an objecting but non-intervening shareholder would be less effective with the trial judge and would have a weaker hand in negotiations with the parties for better settlement terms. Some shareholders might even decide not file objections if they do not have the power of an appeal behind them. Because the system of justice would suffer, the Court should make review by the appellate courts of derivative and class settlements as barrier-free as possible.

D. Requiring a limited form of intervention for purposes of appeal would not fully address the concerns of institutional investors.

One of the issues raised but not resolved by the decision of the Seventh Circuit is whether intervention by an objecting shareholder for purposes of appealing approval of a settlement may be something short of or different from the intervention contemplated by Rule 24. If it may, the full weight of the responsibilities and burdens of intervention described above might not fall on a shareholder intervening for purposes of appeal. For example, the Court possibly could rule that an objecting shareholder must intervene to appeal but that the motion may be perfunctory, no pleading is required, the trial court should grant the motion in all but extraordinary circumstances, and the intervenor has no greater obligation than to pursue an appeal for its own interests.

Even if the Court were to use this case to define the precise scope and consequences of a limited intervention for purposes of appeal with sufficient precision to avoid the continued costs of further lower court litigation over those issues, such an outcome would address some but not all of

the concerns of the Institutional Investors. First, residual risks of bearing the load of a full intervention would remain and would inevitably affect decisions of institutional investors. A shareholder that intervenes to appeal approval of a settlement would retain its position as an intervenor if the appeal is successful and the case is remanded for further proceedings. It would then likely feel pressure from the court or an obligation to continue assisting in the litigation of the case.

Second, if intervention for purposes of appeal is different from standard intervention, requiring an objecting shareholder to engage in the ministerial act of filing a document called a motion to intervene having no significant legal consequences other than permitting an appeal would be an exercise in empty and wasteful formalism.[23] It would add unnecessary legal costs and burdens while serving no legitimate judicial interest.

Third, permitting a limited form of intervention for purposes of appeal would presumably not benefit the Petitioners in this case because they did not seek any form of intervention. Thus, the objectionable settlement reached in this case would remain intact unless the Petitioners have an ability to move for intervention on remand. Finally, although some courts have recognized forms of limited intervention,[24] the terms of the existing statutes and rules do not provide for such a procedure or intervention for purposes

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[23] See Taylor v. Voss, 271 U.S. 176, 187 (1926) (construing a statute to remove "in large measure the technical questions of procedure which has so greatly obstructed its efficient administration, and served in so many instances as a trap, not intended by Congress, to unwary persons enmeshed in abstruse perplexities.").

[24] Moore, supra note –, § 24.23[1].

of appeal. They provide only for full intervention.[25]

II. FEDERALISM AND *ERIE* CONSIDERATIONS FAVOR PERMITTING SHAREHOLDERS TO APPEAL WITHOUT INTERVENING.

States have a strong and legitimate interest in preventing collusive and inadequate settlements of derivative actions because they typically involve state law claims. Several states, including states that frequently are the place of incorporation or derivative litigation, advance that interest by permitting objecting shareholders to appeal without intervening. If it concludes that no federal statute or rule expressly controls the issue in this case, the Court should take these strong state interests into account in determining whether an objecting shareholder in federal court must intervene to appeal. "Otherwise the accident of diversity of citizenship would constantly disturb equal administration of justice in coordinate state and federal courts sitting side by side."[26]

Since *Erie*,[27] federal courts sitting in diversity of citizenship cases have faced a variety of situations requiring this Court to determine the extent to which the federal system should apply state statutes, rules, or law rather than federal procedural statutes or rules. Although that question

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[25] See Amchem, 117 S. Ct. at 2248 (courts must enforce the Federal Rules of Civil Procedure as written).

[26] Klaxon Co. v. Stentor Elec. Mfg. Co., 313 U.S. 487, 496 (1941).

[27] Erie R.R. Co. v. Tompkins, 304 U.S. 64 (1938).

has often been troubling,[28] the Court has consistently interpreted the federal rules with sensitivity to important state interests and regulatory policies.[29] The principle it has followed is that, in the absence of a federal statute or rule directly on point,[30] state requirements that reflect important state policy interests should control in an action based on state law filed in federal court under diversity jurisdiction.[31] The objective is substantial uniformity of predictable outcome between federal and state courts.

For example, in *Walker*, the Court decided that a state rule rather than the federal rule on the time for commencing a civil action determined the date for assessing compliance with a state statute of limitations. Similarly, in *Gasperini*, the Court decided that the *Erie* doctrine required application of a New York statute empowering appellate courts to review the size of jury awards and order new trials when the amount materially deviated from reasonable compensation. It then reconciled the commands of the Seventh Amendment with the state interests protected by the *Erie* doctrine by ordering the federal trial court rather than the federal appellate court to apply the New York statute.

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[28] Walker v. Armco Steel Corp., 446 U.S. 740, 744 (1980).

[29] Gasperini v. Center for Humanities, Inc., 518 U.S. 415, 427 n.7 (1996). See also Richard H. Fallon et al., Hart and Wechsler's The Federal Courts and the Federal System 729 (4th ed. 1996) ("The Supreme Court has continued since [*Hanna v. Plumer*, 380 U.S. 460 (1965)] to interpret the federal rules to avoid conflict with important state regulatory policies."), quoted with approval in Gasperini, 518 U.S. at 437 n.22.

[30] See, e.g., Stewart Org., Inc. v. Ricoh Corp., 487 U.S. 22 (1988); Hanna v. Plumer, 380 U.S. 460 (1965).

[31] See Walker, 446 U.S. at 752.

The Court showed the same concern for accommodating state law interests in shareholder derivative cases brought in federal court. In *Cohen v. Beneficial Industrial Loan Corp.*,[32] the Court, observing that the difference between substantive and procedural rules was not always clear or dispositive, applied a statute of the forum state making certain unsuccessful shareholder plaintiffs liable for the legal fees and expenses of the defense and requiring the plaintiffs to post security for those amounts before the case could proceed. The Court recognized the important state interests underlying derivative cases; it described shareholder derivative actions as creatures of state law and said "the state has plenary power over this type of litigation."[33]

This respect for state interests should inform the Court's resolution of this case. In determining the rule for federal courts sitting in shareholder derivative cases based on diversity of citizenship, the Court should take into account that the practice in states commonly the location of incorporation or derivative actions is not to require intervention to preserve the right to appeal.

The practice in Delaware is particularly important because Delaware is the most favored state of incorporation[34] and is frequently the location of shareholder derivative litigation. Delaware has a trial court rule identical to Rule

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[32] 337 U.S. 541 (1949).

[33] 337 U.S. at 549-50, 555-57. See also Kamen v. Kemper Fin. Servs., Inc., 500 U.S. 90 (1991) (in a derivative action based on a federal claim, the Court decided as a matter of federal common law to incorporate state rules on the need to make a demand on the board and on demand futility rather than create a uniform federal rule).

[34] See Curtis Alva, Delaware and the Market for Corporate Charters: History and Agency, 15 Del. J. Corp. L. 885, 887 (1990).

23.1 and permits an objecting shareholder to appeal without intervening.[35]

Other states that are frequently the place of incorporation or the location of many derivative cases also permit an objecting shareholder or unnamed class member to appeal without first intervening. New York,[36] California,[37] and Illinois[38] are among them.

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[35] Prezeant v. De Angelis, 636 A.2d 915 (Del. 1994) (class action); Kahn v. Sullivan, 594 A.2d 48 (Del. 1991) (class and derivative actions); In re Resorts Int'l, 570 A.2d 259 (Del. 1990) (class and derivative actions).

[36] Jack Weinstein et al., New York Civil Practice: CPLR ¶ 5511.04 (1998) ("In some cases, the standing to appeal of persons who participated but were not technically 'parties' below will be fairly clear. In a stockholder's derivative action, for example, interested stockholders, other than the plaintiffs have been held to have standing to appeal from a judgment adverse to the class.") (citing Auerbach v. Bennett, 393 N.E.2d 994, 998-99 (N.Y. 1979) ("In view of the established rule that a dismissal on the merits of one derivative action is generally a bar to suits by stockholders of the same corporation on the same cause of action, we have no difficulty in recognizing one of the stockholders, who is within the class for whose benefit a derivative action has been instituted, as a party aggrieved by whom a notice of appeal may be filed . . . .") (citations omitted); Posen v. Cowdin, 44 N.Y.S.2d 842 (App. Div. 1943)).

[37] Rebney v. Wells Fargo Bank, N.A., 269 Cal. Rptr. 844, 852 (Ct. App. 1990) ("[A]ll [unnamed class members who object to a settlement] have to do is appear as objectors at the fairness hearing and then take an appeal."); Trotsky v. Los Angeles Fed. Sav. & Loan Assoc., 121 Cal. Rptr. 637, 640 (Ct. App. 1975) (class action); Jon Eisenberg et al., California Practice Guide ¶ 2:274.1 (1997) ("An unnamed class member who is aggrieved by settlement of the class action and who made an appearance to object to the settlement has standing to appeal a judgment approving the settlement.").

[38] Gowdey v. Commonwealth Edison Co., 345 N.E.2d 785 (Ill.

(continued...)

Because a federal intervention requirement would deter institutional investors from appealing and because appeals and the threat of appeals are likely to lead to different results in some cases, the presence of diversity could affect the outcome of a derivative case. That prospect implicates federalism and *Erie* concerns,[39] and therefore, in one of several possible ways, the Court should defer to the state approach. It should apply the relevant state rule governing appeals by objecting shareholders, construe the relevant federal rule to conform to the practice in the important states discussed above and not require intervention, or incorporate the state rule as a federal common law rule.

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[38] (...continued)
App. Ct. 1976) (class action). In Florida, by contrast, objectors must attempt to intervene before appealing. See, e.g., Ramos v. Philip Morris Cos., Inc., 714 So.2d 1146 (Fla. Dist. Ct. App. 1998) (class action).

[39] See Gasperini, 518 U.S. at 431 ("*Erie* precludes a recovery in federal court significantly larger than the recovery that would have been tolerated in state court.").

CONCLUSION

For the foregoing reasons, the Institutional Investors request that the Court reverse the Seventh Circuit and permit the Petitioners to appeal the district court's approval of the settlement in this case without first intervening.

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APPENDIX

LIST OF AMICI CURIAE

The amici curiae joining this brief are:

AFL-CIO Staff Retirement Plan

Barclays Global Investors, N.A.

California State Teachers' Retirement System

Los Angeles County Employees Retirement Association

National Industry Pension Fund

New York City Board of Education Retirement System

New York City Employees' Retirement System

New York City Fire Department Pension Fund

New York City Police Department Pension Fund

New York City Teachers' Retirement System

New York State Common Retirement Fund

New York State Teachers' Retirement System

State of Wisconsin Investment Board

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OCTOBER TERM, 1998

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM and FLORIDA STATE BOARD OF ADMINISTRATION,

Petitioners,

v.

PAUL FELZEN, et al.,

Respondents.

On Writ of Certiorari to the
United States Court of Appeals for the Seventh Circuit

BRIEF AMICUS CURIAE OF PUBLIC CITIZEN, INC., AND TRIAL LAWYERS FOR PUBLIC JUSTICE IN SUPPORT OF PETITIONERS

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34 pp

TABLE OF CONTENTS

TABLE OF AUTHORITIES iii

INTEREST OF AMICI 1

STATEMENT OF THE CASE 3

SUMMARY OF ARGUMENT 4

ARGUMENT 7

INTERVENTION IS NOT REQUIRED BEFORE AN APPEAL MAY BE TAKEN FROM A SETTLEMENT APPROVED UNDER RULES 23 AND 23.1 7

A. The Decisions That Inspired Adoption Of The Intervention Requirement—*Marino* And *Guthrie*—Do Not Support An Intervention Requirement For Class Members Who Timely File Objections To Class Action Settlements. 7

1. *Marino v. Ortiz* Provides No Support For Respondents. 7

2. *Guthrie* Is Factually Distinguishable And Wrongly Decided. 11

B. The Intervention Requirement Undermines The Role of Objectors In Assuring Fair And Non-Collusive Class Action Settlements. 17

C. Requiring Intervention Is A Trap For Unwary Class Members. 24

CONCLUSION 26

TABLE OF AUTHORITIES

PAGE(S)

CASES

Alaska v. Suburban Propane Gas Corp.,
123 F.3d 1317 (9th Cir. 1997) 18-19

Amchem Products, Inc. v. Windsor,
117 S. Ct. 2231 (1997) 1, 14, 15, 23

American Pipe and Construction Co. v. Utah,
414 U.S. 538 (1974) 5, 9

Bowling v. Pfizer, 922 F. Supp. 1271 (S.D. Ohio),
aff'd, 102 F.3d 777 (6th Cir. 1996) 1

Bowling v. Pfizer, Inc., 132 F.3d 1147 (6th Cir. 1998) 20

Bradley v. Milliken, 828 F.2d 1186 (6th Cir. 1987) 20

In re Brand Name Prescription Drugs Antitrust Litigation,
115 F.3d 456 (7th Cir. 1997) 6, 16, 19

Croydon Associates v. Alleco, Inc.,
969 F.2d 675 (8th Cir. 1992),
cert. denied, 507 U.S. 908 (1992) 9, 12

Eisen v. Carlisle and Jacquelin, 417 U.S. 156 (1974) 16

Felzen v. Andreas,
134 F.3d 873 (7th Cir. 1998) 4, 8, 19, 24

In re Ford Motor Co. Bronco II Product Liability Litig.,
1995 U.S. Dist. LEXIS 3507
(E.D. La. Mar. 20, 1995) 1

In re General Motors Corp. Engine Interchange Litigation,
594 F.2d 1106 (7th Cir.), *cert. denied*,
444 U.S. 870 (1979) 10, 15

In re General Motors Corp. Pick-up Truck Fuel Tank Litigation, 55 F.3d 768 (3d Cir.), *cert. denied*,
116 S. Ct. 88 (1995) 1, 6, 20, 23

General Telephone Co. of the Southwest v. Falcon,
457 U.S. 147 (1982) 21

Georgine v. Amchem Products, Inc.,
83 F.3d 610 (3d Cir. 1996) 23

Gottlieb v. Wiles, 11 F.3d 1004 (10th Cir. 1993) 7

Guthrie v. Evans, 815 F.2d 626 (11th Cir. 1987) ..... *passim*

Hansberry v. Lee, 311 U.S. 32 (1940) 15

Marino v. Ortiz, 484 U.S. 301 (1988) 4, 7, 8, 9

Mars Steel Corp. v. Continental Ill. Nat'l Bank & Trust Co.,
834 F.2d 677 (7th Cir. 1987) 22

Martin v. Wilks, 490 U.S. 755 (1989) 11, 20-21

Matsushita Electric Industrial Co. v. Epstein,
516 U.S. 367 (1996) 5, 11, 15, 21

Phillips Petroleum Co. v. Shutts,
472 U.S. 797 (1985) 5, 10, 11, 17, 21

Shults v. Champion International Corp.,
35 F.3d 1056 (6th Cir. 1994) 7, 17

Trbovich v. United Mine Workers of America,
404 U.S. 528 (1972) 17

United Airlines, Inc. v. McDonald,
432 U.S. 385 (1977) 18, 19

Wade v. Goldschmidt, 673 F.2d 182 (7th Cir. 1982) 20

Walker v. City of Mesquite,
858 F.2d 1071 (5th Cir. 1988) 7, 9, 12, 14

Walker v. Liggett Group, Inc.,
175 F.R.D. 226 (S.D. W.Va. 1997) 2

Weinberger v. Great Northern Nekoosa Corp.,
925 F.2d 518 (1st Cir. 1991) 22

Zahn v. International Paper Co., 414 U.S. 291 (1973) ... 5, 9

STATUTES AND RULES

28 U.S.C. 1291 19

28 U.S.C. 1332 9

Fed. R. Civ. P. 23 ..... 2, 4, 5, 17, 19, 23, 24

Fed. R. Civ. P. 23(a)(2) 21

Fed. R. Civ. P. 23(a)(3) 21

Fed. R. Civ. P. 23(a)(4) 13, 16, 20

Fed. R. Civ. P. 23(b)(3) 16

Fed. R. Civ. P. 23(c)(2) 12, 15, 16

Fed. R. Civ. P. 23(d) 12

Fed. R. Civ. P. 23(e) 10, 12, 16, 22

Fed. R. Civ. P. 23.1 ..... 2, 3, 4, 5, 12, 24

Fed. R. Civ. P. 24 ..... 6, 7, 18, 20, 21, 25

Fed. R. Civ. P. 24(a) 10, 21

Fed. R. Civ. P. 24(b) 21

Fed. R. Civ. P. 24(c) 21

Fed. R. Civ. P. 26(b)(1) 10

Fed. R. Civ. P. 27 10

Fed. R. Civ. P. 33 10

Fed. R. Civ. P. 34 10

MISCELLANEOUS

Duffy, *The Appealability of Class Action Settlements by Unnamed Parties*, 60 Univ. Chi. L. Rev. 933 (1993) .. 18

Empirical Study of Class Actions in Four Federal District Courts (Federal Judicial Center 1996) 23

Kahan & Silberman, *The Inadequate Search for 'Adequacy' in Class Actions: A Critique of Epstein v. MCA, Inc.*, 73 N.Y.U. L. Rev. 765 (1998) 15

Koniak, *Feasting While The Widow Weeps: Georgine v. Amchem Products, Inc.*, 80 Cornell L. Rev. 1045 (1995) 23

Koniak & Cohen, *Under Cloak of Settlement*, 82 U. Va. L. Rev. 1051 (1996) 23

Manual on Complex Litigation Third, (Federal Judicial Center 1995) 10, 13, 22, 24, 25

H. Newbert & A. Conte, *Newberg on Class Actions* (3d ed. 1992) 5, 6, 10

Reske, "Two Wins for Class Action Objectors," 82 A.B.A. Journal 36 (June 1996) 1

INTEREST OF AMICI[1]

Public Citizen was founded in 1971 as a public advocacy, lobbying, and litigating organization. On behalf of its 100,000 members, Public Citizen has worked on issues involving corporate responsibility toward shareholders such as those presented in the suit before this Court. It also believes strongly in the need for class actions to effectively enforce consumer and shareholder rights because individuals acting alone often do not have the means to do so, and it has frequently made use of the class device on behalf of consumers. Public Citizen recognizes, however, that class actions can be abused, to the detriment of the class members. Thus, through its Litigation Group, Public Citizen has represented objectors in approximately 30 nationwide class action settlements in which the named representatives and their attorneys were inattentive to the needs and divergent interests of the absent class members whom they were supposed to represent.[2] Public Citizen opposes the result sought by respondents here because it would

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[1] Letters of consent to the filing of this brief have been lodged with the Clerk. Pursuant to Rule 37.6 of this Court, *amici* state that no party had any role in writing this brief and that no one other than *amici* made a monetary contribution to its preparation or submission.

[2] *See, e.g., Amchem Prods., Inc. v. Windsor*, 117 S. Ct. 2231 (1997); *In re General Motors Corp. Pick-up Truck Fuel Tank Litig.*, 55 F.3d 768 (3d Cir.), *cert. denied*, 516 U.S. 824 (1995); *Bowling v. Pfizer*, 922 F. Supp. 1271 (S.D. Ohio), *aff'd*, 102 F.3d 777 (6th Cir. 1996); *In re Ford Motor Co. Bronco II Prod. Liab. Litig.*, 1995 U.S. Dist. Lexis 3507 (E.D. La. Mar. 20, 1995); *see generally* Reske, "Two Wins for Class Action Objectors," 82 A.B.A. Journal 36, 37 (June 1996) (highlighting Public Citizen's work representing objecting class members).

undermine the ability of objecting class members to appeal the approval of improper class action settlements, thus curtailing an important tool for curbing class action abuse.

Trial Lawyers for Public Justice ("TLPJ") is a national public interest law firm dedicated to pursuing justice for people harmed by corporate and governmental abuses. TLPJ prosecutes cases throughout the federal and state courts to advance consumers' rights, environmental protection and safety, civil rights and civil liberties, occupational health and employees' rights, the preservation and improvement of the civil justice system, and the protection of the poor and powerless. TLPJ believes that class actions are essential and has brought them in many areas ranging from sex discrimination to consumer rights. However, class actions can be abused and turned into a tool for curtailing rights. Thus, TLPJ has established a Class Action Abuse Prevention Project to monitor, expose, and prevent abuses of the class action device. In this capacity, TLPJ often serves as counsel for class members who object to unlawful or unfair class action settlements. *See, e.g., Walker v. Liggett Group, Inc.*, 175 F.R.D. 226 (S.D. W.Va. 1997). TLPJ is concerned that requiring intervention as a condition for appellate standing will restrict the availability of appellate review of class action settlements. This restriction on appellate review, in turn, will increase the potential for unfair, collusive settlements that are not in the best interests of the class.

This case involves the settlement of shareholder derivative suits under Federal Rule of Civil Procedure 23.1, and thus petitioners will focus on the specifics of that Rule. *Amici*, on the other hand, will focus primarily on the settlement process under the closely related class action provisions of Rule 23, where the need for protection of the class, and the dangers of erecting procedural barriers of the kind created by the Seventh

Circuit below, are, if anything, of greater significance.

STATEMENT OF THE CASE

This case arises from a series of shareholder derivative actions brought on behalf of Archer Daniels Midland Company ("ADM"), a large agricultural corporation. Those actions piggybacked on a federal investigation that led to a guilty plea and a $100 million criminal fine paid by ADM for conspiring with its competitors to fix the prices of its agricultural products. The suits alleged that ADM's directors breached their fiduciary duties by failing to oversee the company's operations properly, and they sought recovery on behalf of the company of the $100 million criminal fine, plus $90 million that ADM had paid to settle related civil antitrust suits. *See* Petition at 5.

According to petitioners, plaintiffs' counsel allowed the derivative actions to languish for nearly two years without taking meaningful discovery. *Id.* at 6. Thereafter, a settlement was reached, which simply incorporated alleged corporate reform measures that ADM's directors had already adopted. The only cash component of the settlement—$8 million—went to pay attorney's fees, half for the plaintiffs' lawyers and the other half to pay the future fees to be expended by ADM in its supposed reform efforts. *Id.*

After the settlement was proposed, ADM shareholders were notified of the terms of the settlement and their right to object to it, as required by Federal Rule of Civil Procedure 23.1. Petitioners, two large public pension funds with significant stock holdings in ADM, filed written objections and appeared through counsel at a hearing to determine whether the settlement should be approved, arguing that the settlement provided no real benefits except to the lawyers and thus "sold out" the interests

of the corporation. However, petitioners did not move to intervene in the actions. *See* Petition at 7. The district court approved the settlement, and petitioners appealed.

The Seventh Circuit dismissed the appeal. Although this case involves a derivative action under Rule 23.1, the court began by holding that unnamed class members may not appeal the approval of a Rule 23 class action settlement unless they have intervened in the action. Pet. App. 4a, *Felzen v. Andreas*, 134 F.3d 873, 875 (7th Cir. 1998). Based largely on that conclusion, the court of appeals then held that shareholders in a derivative action must also have first intervened before they may appeal the approval of a settlement. *Id.* at 875-76. Because petitioners had not moved to intervene, the court dismissed the appeal. In reaching that result, the Seventh Circuit panel overruled four of its prior decisions, claiming reliance on the intervening ruling of this Court in *Marino v. Ortiz*, 484 U.S. 301 (1988) (per curiam).

SUMMARY OF ARGUMENT

A. As the Seventh Circuit's decision recognized, the question of appealability in the Rule 23 context is closely related to appealability in a Rule 23.1 derivative action, and thus it is likely that the decision of this Court will answer the Rule 23 issue as well. *See* Petition at 12 n.10. But there is a difference between the two issues. As petitioners' question presented acknowledges, shareholders who object to a settlement in a derivative action are not, technically speaking, "parties" to the action, which is brought on behalf of the corporation. The shareholders do, however, have a direct interest in the action, since the suit seeks to recover assets for a corporation that they, in part, own. That is precisely why Rule 23.1 requires that shareholders be notified of the settlement of any derivative

action and why they are given the right to object to the settlement. Thus, we fully agree with petitioners that shareholders are "privies" to the plaintiffs in a derivative action and that requiring them to intervene before they may appeal is contrary to Rule 23.1 and common-law practice, and would undermine the efforts of shareholders to monitor derivative litigation. Petition at 17-23.

Unnamed class members in a Rule 23 class action do not face the same technical problem as that faced by Rule 23.1 shareholders, and thus, as applied to them, the intervention requirement is even more inappropriate. Unnamed class members need not intervene because, in key respects, they are *already* parties to the action by virtue of their class membership. Although unnamed class members are treated differently from named plaintiffs for some purposes, *see* H. Newberg & A. Conte, 1 *Newberg on Class Actions* § 1.04 (3d ed. 1992), they are treated as parties in many respects, for example, for statute of limitations purposes, *American Pipe and Construction Co. v. Utah*, 414 U.S. 538, 551 (1974), and for determining subject matter jurisdiction. *Zahn v. International Paper Co.*, 414 U.S. 291 (1973). Most importantly, class members are treated as parties insofar as their claims are released by a properly approved class settlement. Thus, it is illogical and unfair to require class members to intervene in order to appeal from a class action settlement, when, with respect to its most significant practical consequence—its binding effect—they are already parties to the action. *See Matsushita Elec. Indus. Co. v. Epstein*, 516 U.S. 367 (1996); *Phillips Petroleum Co. v. Shutts*, 472 U.S. 797, 811-12 (1985).

B. An intervention requirement would undermine the role of objectors in assuring fair and non-collusive class action settlements. Some courts have suggested that allowing absent

class members or shareholders in a derivative action to appeal would create intolerable inefficiency, and that, therefore, intervention should be allowed only where the objecting class member can show that the named plaintiffs are not adequate class representatives. *See, e.g., In re Brand Name Prescription Drugs Antitrust Litig.*, 115 F.3d 456, 457 (7th Cir. 1997). That standard makes no sense because a class action settlement is subject to challenge for a host of reasons unrelated to the class representatives' adequacy, including that its benefits are not sufficient. *See, e.g., In re General Motors Corp. Pick-up Truck Fuel Tank Litig.*, 55 F.3d 768, 804-18 (3d Cir.), *cert. denied*, 116 S. Ct. 88 (1995); H. Newberg & A. Conte, 2 *Newberg on Class Actions* § 11.58 (3d ed. 1992) (detailing wide range of types of objections). Therefore, an adequacy of representation standard would effectively insulate many class settlements from appellate review and create an atmosphere in which unfair or collusive class action settlements could flourish.

C. An intervention requirement would also harm class members by creating a trap for the unwary. When class actions are settled, notice and an opportunity to object is provided to the absent class members who, generally speaking, do not have lawyers. Requiring such *pro se* class members to intervene under Rule 24 would likely cut off their rights to appeal because they would probably not know of such a requirement and, even if they did, they would not know how to comply with it. Moreover, requiring formal intervention adds nothing to the process, which already requires objectors to state their particular objections before the district court and only those objections can be raised on appeal.

ARGUMENT

INTERVENTION IS NOT REQUIRED BEFORE AN APPEAL MAY BE TAKEN FROM A SETTLEMENT APPROVED UNDER RULES 23 AND 23.1

A. The Decisions That Inspired Adoption Of The Intervention Requirement — *Marino* And *Guthrie* — Do Not Support An Intervention Requirement For Class Members Who Timely File Objections To Class Action Settlements.

A body of case law holds that an absent class member does not have "standing" to appeal a district court's approval of a class action settlement unless he or she has intervened under Federal Rule of Civil Procedure 24. *See, e.g., Shults v. Champion Int'l Corp.*, 35 F.3d 1056 (6th Cir. 1994); *Gottlieb v. Wiles*, 11 F.3d 1004 (10th Cir. 1993); *Walker v. City of Mesquite*, 858 F.2d 1071 (5th Cir. 1988). Two cases—*Marino v. Ortiz*, 484 U.S. 301 (1988) (per curiam), and *Guthrie v. Eva...*, 815 F.2d 626 (11th Cir. 1987)—have led to this development. As we now show, the actual holdings and rationales of *Marino* and *Guthrie* do not support an intervention requirement.

1. *Marino v. Ortiz* Provides No Support For Respondents.

In *Marino*, a class consisting of black and Hispanic police officers sued the New York Police Department under Title VII of the Civil Rights Act, alleging that a police sergeant's examination was discriminatory. Thereafter, the case settled, and a group of white police officers, who were not class

members and who had not sought to intervene, appeared at the final fairness hearing on the settlement and presented their objections to the settlement. The district court approved the settlement, and the group of whites appealed. On appeal, the Second Circuit affirmed, not on the merits of the settlement, but on the ground that the appellants were not parties to the action.

This Court affirmed in a three-paragraph per curiam opinion. The non-intervening white officers' appeal could not be maintained, the Court held, under the "well settled" principle "that only parties to a lawsuit, or those that properly become parties, may appeal an adverse judgment." *Marino*, 484 U.S. at 304. Responding to the Second Circuit's suggestion that there might be some exception to this general principle, the Court disagreed, noting that "the better practice is for such a *nonparty* to seek intervention for purposes of appeal." *Id.* (emphasis added).

Marino does not support imposing an intervention requirement on class members who object to a class action settlement. The white police officers were not members of the class of black and Hispanic officers who had sued the police department, and they did not move to intervene. It was those key facts—that the appellants were not class members and they had not sought party status through intervention—that led this Court to affirm the dismissal of the appeal, leaving the implication that, had the appellants been class members, no intervention would have been necessary. Indeed, if, under *Marino*, even class members must seek intervention in order to appeal, as the court below held, Pet. App. 3a, *Felzen*, 134 F.3d at 875, the Court's contrasting depiction of the black and Hispanic *plaintiff* class members with the *non-party* white officers would have been superfluous. *Marino*, 484 U.S. at 303. Thus, if anything, *Marino* supports our view that absent class

members are already "parties" who need not intervene to appeal from approval of a class action settlement that directly affects their own rights by barring future suits on the claims covered by the settlement.

In imposing an intervention requirement, the lower courts have ignored *Marino*'s facts and adopted the following syllogism: Absent class members are "non-parties" and *Marino* requires intervention for "non-parties" before they may appeal. *Croydon Assocs. v. Alleco, Inc.*, 969 F.2d 675, 679 (8th Cir. 1992), *cert. denied*, 507 U.S. 908 (1992); *Walker*, 858 F.2d at 1074. But the premise of that syllogism is wrong. Although the rights and obligations of named plaintiffs and of unnamed plaintiff class members differ in some important respects, decisions of this Court and other authorities demonstrate that both named and unnamed plaintiffs are "parties" for all purposes relevant to whether intervention is a precondition for appellate standing.

For instance, in holding that class members' statutes of limitations, like those of the named plaintiffs, are tolled during the pendency of a class action, this Court relied on the fact that absent class members are "parties to the suit." *American Pipe and Construction Co. v. Utah*, 414 U.S. 538, 551 (1974). Moreover, the claims of non-named plaintiffs, like those of named plaintiffs, must meet the requisite jurisdictional amount in diversity cases under 28 U.S.C. 1332. *Zahn v. International Paper Co.*, 414 U.S. 291 (1973).

In addition, the role that absent class members play as objectors to class settlements is based on the fact that they have a direct interest in the claims asserted in the litigation, which are assumed to be equal in stature to those of the named plaintiffs. Thus, they are given notice of the settlement and they must

come forward to assert their rights, or they will be foreclosed from doing so in the future. *See* Fed. R. Civ. P. 23(e); *Manual on Complex Litigation Third*, § 30.41, at 236-38 (Federal Judicial Center 1995) (hereafter "Manual"). On the other hand, by definition, under Rule 24(a), non-parties who seek intervention do *not* have rights at stake in the suit that can be legally affected by the situation. Instead, they must prove their interest in the controversy before they achieve party status. *See* Fed. R. Civ. P. 24(a).

Furthermore, absent class members are often allowed discovery into the justification for a class settlement, precisely because of their undisputed interest in the litigation. H. Newberg & A. Conte, 2 *Newberg on Class Actions* § 11.57 (3d ed. 1992); *see, e.g., In re General Motors Corp. Engine Interchange Litig.*, 594 F.2d 1106, 1126 (7th Cir.), *cert. denied*, 444 U.S. 870 (1979). Since under the Federal Rules of Civil Procedure, discovery may be obtained only by parties to the action, or those expecting to become parties, Fed. R. Civ. P. 27, it is clear that the courts view absent class members as parties for discovery purposes. *See* Fed. R. Civ. P. 26(b)(1) ("*Parties* may obtain discovery" regarding relevant, non-privileged matters), Fed. R. Civ. P. 33 ("*any party* may serve upon any other party written interrogatories"), Fed. R. Civ. P. 34 ("*Any party* may serve upon any other party" document requests).

Most fundamentally, an absent class member is a party for *res judicata* purposes. Thus, a judgment approving a class action settlement has binding effect on that class member, even if the judgment is entered in a court on the other side of the continent with which the class member has no contact, *Phillips Petroleum Co. v. Shutts*, 472 U.S. 797, 811-12 (1985), and even if the judgment releases the class member's claims and potential claims on a far-reaching, global basis. *See Matsushita Elec.*

Indus. Co. v. Epstein, 516 U.S. 367 (1996). To be sure, because the vicarious nature of class representation raises concerns not present in traditional bi-polar litigation, absent class members may only be bound to a judgment after minimal due process safeguards—such as notice, adequate representation, and opt-out rights—are provided. *Shutts*, 472 U.S. at 812. But if those procedures are followed, the absent class members have had their "day in court," *Martin v. Wilks*, 490 U.S. 755, 762 (1989), and the judgment binds them as "parties" just as assuredly as it does the named plaintiffs. Conversely, non-class members, such as the white police officers in *Marino*, would not be bound by a settlement, precisely because they are not parties to the litigation. *See id.* at 762-65. Accordingly, it is unfair and illogical to require class members to surmount the additional burden of intervention when they seek to protect their rights by appealing an adverse judgment.

2. *Guthrie* Is Factually Distinguishable And Wrongly Decided.

The other key decision leading to widespread adoption of the intervention rule—*Guthrie v. Evans*, 815 F.2d 626 (11th Cir. 1987)—involves very different facts from those involved in class action settlements, and thus does not support an intervention requirement. In addition, as explained below, *Guthrie*'s policy justifications for the intervention rule do not survive analysis.

Guthrie was a suit challenging conditions at a state prison. After 13 years of contested litigation, the district court issued a permanent injunction prohibiting the defendants from violating prior court orders. An inmate-class member who, so far as the opinion reveals, never participated in the district court proceedings, appealed the injunction. *Id.* at 627. The Eleventh

Circuit dismissed the appeal, holding that an unnamed individual class member does not have standing to appeal a final class action judgment. Although the court's holding was stated in broad terms, *Guthrie* suggested that the right to appeal might be treated differently "when there is disagreement among members of the class on settlements." *Id.* Unfortunately, cases following *Guthrie* and overlooked the fact that *Guthrie* was a litigated, not a settled, case. *See, e.g., Walker*, 858 F.2d at 678; *Croydon Assocs.*, 969 F.2d at 1073.

Whether and by what means an unnamed plaintiff who objects to a class action settlement may appeal is quite different from whether, as in *Guthrie*, a class member may appeal after a class action has been litigated to judgment. In the litigation situation, an unnamed class member generally has been notified of the action prior to trial, *see* Fed. R. Civ. P. 23(c)(2), (d), and, usually, as apparently was the case in *Guthrie*, has not asserted her rights at any time prior to judgment. Thus, the *Guthrie*-type absentee has given neither the court nor the other parties notice of her intent to appear, of what arguments she might raise, or of how her interests differ from those of the named plaintiffs. Whether described as lack of appellate "standing," *Guthrie*, 815 F.2d at 627, or as a failure to intervene and object below, the essential problem is one of unfair surprise, and thus is akin to the ordinary prohibition against raising on appeal issues that have not been raised in the district court.

The situation presented by class action settlements is altogether different from that presented by *Guthrie*. In the settlement context, absent class members respond to a notice required by the Federal Rules. *See* Fed. R. Civ. P. 23(e), 23.1. The very purpose of the notice is to call forth objections and to assure that the court is presented with arguments that expose the potential pitfalls, as well as the benefits, of the settlement by

persons who have an undisputed interest in the case. Manual, § 30.41, at 237. As occurred in the settlement of the derivative actions here, this notice is generally the first time that the class members learn of the action. *See id.* (in settlement class actions, notice of pendency of action and of settlement is simultaneous). Among other things, the class members (or the shareholders in a derivative action) are told that they may file objections to the settlement by a specific date, and appear in person at a district court hearing to determine whether the settlement should be approved as fair, adequate, and reasonable. *See id.* § 41.43, at 488 (model class action settlement notice). To our knowledge, such notices never mention a need for intervention. If the objectors do not persuade the district court, at least they will have alerted the settling parties and the court of their specific positions on the matter, and thus an appeal surely will not come as a surprise.

Thus, *Guthrie*'s facts are a far cry from the facts here or in settlement class actions generally. Nonetheless, other courts have relied on the policy rationales offered by *Guthrie* to support imposition of a broad intervention requirement. As we now show, none of those rationales withstands scrutiny.

a. *First, Guthrie* asserted that because the class member who sought to upset the district court's injunction had not obtained a finding from the district court that he would adequately protect the interests of the class, he "clearly has no standing to take any action on behalf of the class." 815 F.2d at 628. That rationale is a non-sequitur, at least as it applies to challenges to class action settlements.

Before a class can be certified and a settlement approved, named plaintiffs and their counsel must be found to be adequate representatives under Rule 23(a)(4). *See Amchem*

Prods., Inc. v. Windsor, 117 S. Ct. 2231, 2250-51 (1997). But that has nothing to do with the role of an objector, who claims not to represent the class but that the settlement is unfair to him (and to others similarly situated). Indeed, objectors often maintain that the named representatives are inadequate, or that *no one* is an adequate representative because of inherent class conflicts, as this Court held just two Terms ago, when it rejected the *Amchem* class action settlement involving a "sprawling" class of millions of people exposed to asbestos. *Id.* at 2250. Further, this argument is not a reason to deny an objector standing to appeal, since, if an objector were required to show that he were an adequate class representative, that would generally bar not only an appeal of the settlement's approval, but any challenge to the fairness of the settlement in the district court as well.

b. *Second*, *Guthrie* and its progeny have denied objectors the right to appeal on the ground that objectors have alternative avenues for relief. 815 F.2d at 628; *see also, e.g.*, *Walker*, 858 F.2d at 1073-74. These courts have relied principally on the right of class members to seek intervention, but that only begs the question presented: whether such intervention is necessary where, as here, the objecting class member has timely appeared in the district court and has put the settling parties on notice of her particular objections.

Guthrie also suggested that collateral attack—the filing of a separate, post-judgment lawsuit attacking the validity of the settlement—is a viable alternative to appeal. 815 F.2d at 628. But that approach is unfair to class members and undermines the interests of the litigants and the courts in finality. Under the law of judgments, an absent class member would be entitled to collaterally attack a judgment approving a class action settlement where due process was the basis of the attack, *see*

Matsushita Elec. Indus. Co. v. Epstein, 516 U.S. 367, 398-99 (1996) (Ginsburg, J., concurring in part and dissenting in part); *cf. Hansberry v. Lee*, 311 U.S. 32 (1940); however, that tool would not be available to challenge the fairness of the settlement or other legal impediments that generally can be contested on direct review. *See, e.g., Amchem*, 117 S. Ct. at 2249-51 (rejecting settlement class action for failure to meet Rule 23 certification criteria). That being the case, a collateral attack is a poor substitute for a direct appeal that can protect all of the absentees' legal interests. *See generally* Kahan & Silberman, *The Inadequate Search for 'Adequacy' in Class Actions: A Critique of Epstein v. MCA, Inc.*, 73 N.Y.U. L. Rev. 765, 780 & n.69 (1998) (hailing superiority of comprehensive direct review over collateral attack and criticizing intervention requirement as potential impediment to appellate review). Moreover, regardless of the scope of collateral attack, it is generally preferable to have challenges to a class action settlement heard in the original forum, with direct appellate review, rather than to encourage each class member to file a separate suit, in a distant forum, challenging the *res judicata* effect of a previously-entered class action judgment.

Guthrie also suggested that because class members have the right to opt out of damages actions certified under Rule 23(b)(3), they do not need appellate review of class action settlements to which they object. 815 F.2d at 628; *see* Fed. R. Civ. P. 23(c)(2). That rationale does not help respondents here, because, in Rule 23.1 derivative actions, there is no right to opt out. More importantly, even in Rule 23(b)(3) cases, the courts have recognized that the right to opt-out is often illusory, because the claims of individual class members are not sufficiently large to support separate litigation. *See, e.g., In re General Motors Corp. Engine Interchange Litig.*, 594 F.2d at 1136. Indeed, because one of the principal purposes of Rule

23(b)(3) is to allow the aggregation of relatively small claims, it is no answer to say that absent class members who want to appeal approval of a class action settlement could have opted out.

This "love it or leave it" approach to Rule 23 is also at odds with the structure of the Rule, which demands that (b)(3) classes meet the certification criteria, including adequacy of representation, that class members be given opt-out rights, *and* that there be notice and court approval before a settlement can be imposed on class members. Fed. R. Civ. P. 23(a)(4), (c)(2), (e). This reading of the Rule—that its commands are consecutive, not alternative—is confirmed by the logic of *Eisen v. Carlisle and Jacquelin*, 417 U.S. 156 (1974), where the named plaintiffs argued that they should be excused from giving class members notice and opt-out rights under Rule 23(c)(2) because "adequate representation, rather than notice, is the touchstone of due process in a class action...." *Id.* at 176. "[T]his view has little to commend it," the Court held, because "Rule 23 speaks to notice as well as to adequacy of representation and requires that both be provided." *See also id.* at 176 n.13 (class members' opt-out rights also protected). So too here, the right to opt out does not diminish the class members' rights to object to a settlement before the district court and to appeal from an adverse ruling if the settlement is approved.

c. *Third*, and finally, *Guthrie* and its progeny assert that "denying the right to appeal" is necessary to maintain the efficiency of class litigation. *Guthrie*, 815 F.2d at 629; *see also, e.g., In re Brand Name Prescription Drugs Antitrust Litig.*, 115 F.3d 456, 457-58 (7th Cir. 1997). That argument has some force in cases like *Guthrie* that were litigated, but it makes no sense to argue that it is necessary to squelch opposition to class

action settlements because of the concern that they might be overturned, requiring the once-settled case to return to the litigation mode. *See id.* At bottom, this argument proves too much. It would always be expedient to deny class members the right to challenge a class action settlement—in the district court as well as on appeal—but that result would fly in the face of Rule 23 and due process. *See Shutts*, 472 U.S. at 812 (enumerating due process prerequisites to obtain judgment that binds absent class members). In sum, there is no basis to circumscribe an unnamed class member's right to appeal.

B. The Intervention Requirement Undermines The Role of Objectors In Assuring Fair And Non-Collusive Class Action Settlements.

The courts that require class members to intervene have taken two general approaches to the standards by which a motion to intervene will be judged. Some courts suggest that intervention will be granted as a matter of course, *see, e.g., Shults*, 35 F.3d at 1061, and others suggest that intervention will be granted only to class members who can prove that the class representatives are inadequate. *See, e.g., Guthrie*, 815 F.2d at 628.

1. Under the first approach, it is assumed that unnamed class members who are aware of the intervention requirement will file papers explaining the obvious fact that their interests are at odds with those of the settling parties and that they desire intervention solely to protect their appellate standing. *Cf. Trbovich v. United Mine Workers of America*, 404 U.S. 528, 538 & n.10 (1972) (requirement for intervention as of right under Rule 24(a) is met where representation "may be" inadequate, and "burden of making that showing should be treated as minimal") (citation omitted). If that is the operating

assumption, the district judge will be hard pressed not to grant intervention, since to do otherwise would be tantamount to denying the objector's right to appeal. Under this view of the intervention requirement, a Rule 24 motion is little more than additional work for both litigants and judges, with no countervailing benefit, and a potential trap for unwary objectors, particularly *pro se* objectors, who may not know of the need to intervene. *See infra* Part C (discussing burden on *pro se* class members); *see also* Duffy, *The Appealability of Class Action Settlements by Unnamed Parties*, 60 Univ. Chi. L. Rev. 933, 954 (1993) (intervention requirement "produces more work for the district court (a formal motion in addition to the settlement hearing), no savings of time for the appellate court (in both cases it has conducted an appeal) and results in no review of the much more basic issue (the fairness and reasonableness of the settlement) by either court").

Nonetheless, if this Court decides that there is such a requirement, we believe that treating intervention as a formality follows *a fortiori* from *United Airlines, Inc. v. McDonald*, 432 U.S. 385, 392-96 (1977). In that case, the question was whether unnamed class members should be permitted to intervene *after judgment* solely for the purpose of appealing an order denying class certification, which the named plaintiffs had decided not to appeal. If intervention had been denied, the individual absent class members would not have been bound by the judgment, since it did not extend to the merits, but only prevented the named plaintiffs from representing the class. Nonetheless, the Court held that the lower court's denial of intervention was erroneous *as a matter of law*, noting that the defendant was in the same situation regardless of whether the appeal was brought by an unnamed plaintiff rather than by one of the named plaintiffs. *United Airlines*, 432 U.S. at 394; *see also Alaska v. Suburban Propane Gas Corp.*, 123 F.3d 1317

(9th Cir. 1997) (overruling district court's denial of unnamed class member's request to intervene solely for the purpose of appeal). The consequence of denial of intervention is far more severe here than was the case in *United Airlines*. If intervention is denied to a class member seeking to appeal from a settlement, that class member *is* bound by a judgment on the merits. Thus, if intervention is a precondition for appellate standing, it should, under *United Airlines*, be granted as a matter of course to all objectors who have filed timely objections in the district court.

2. The second strain of case law regarding the standard for intervention is of much more concern to *amici* because it strongly implies that class members' rights to appeal will be greatly circumscribed. In *Guthrie*, for instance, the Eleventh Circuit noted, albeit not in the context of a settled case, that "[i]f each class member could appeal individually, the litigation would become unwieldy. Thus, allowing direct appeals by individual class members who have not intervened in the district court would defeat the very purpose of class action lawsuits." 815 F.2d at 629. The court of appeals below made the same point in the settlement context, Pet. App. 4a, *Felzen*, 134 F.3d at 875, relying on its earlier ruling in *Brand Name Prescription Drugs*, which concluded that allowing class members "to appeal would be an ... affront to intelligent judicial administration because it would fragment control of the class action." 115 F.3d at 457.

Although no case of which we are aware sets forth a precise standard by which intervention will be judged, some cases imply that class members will be denied intervention unless they can show that the certified class representative does not adequately represent the interests of the class. *Id.* at 457-58; *Guthrie*, 815 F.2d at 628. Thus, without any basis in Rule 23 or 28 U.S.C. 1291, which provides litigants an appeal as of right

from final decisions in civil cases, the district court would become the court of appeals' gatekeeper. Under that standard, the district court, having already approved the class settlement and, thus, by definition, having found that the class representatives were adequate, *see* Fed. R. Civ. P. 23(a)(4), would almost surely deny intervention. *See, e.g., Wade v. Goldschmidt*, 673 F.2d 182, 186 n.7 (7th Cir. 1982) (an applicant for intervention fails to meet burden of demonstrating inadequate representation "when no collusion is shown between the representative and an opposing party"). At that juncture, the class member would be required to appeal both from approval of the settlement and the denial of intervention, subject, presumably, to abuse of discretion review, which would likely be a difficult standard to meet in the intervention context. *See, e.g., Bradley v. Milliken*, 828 F.2d 1186, 1194 (6th Cir. 1987).

This approach to intervention is seriously mistaken for three related reasons. First, it would effectively reduce the merits of the class settlement to one issue—adequacy of representation, *see* Fed. R. Civ. P. 23(a)(4)—although there are many other legitimate bases for overturning a class settlement or its fees component. *See, e.g., In re General Motors Corp. Pick-up Truck Fuel Tank Litig.*, 55 F.3d 768 (3d Cir.), *cert. denied*, 516 U.S. 824 (1995) (settlement's benefits not fair exchange for release of class members' claims); *Bowling v. Pfizer, Inc.*, 132 F.3d 1147 (6th Cir. 1998) (excessive attorney's fees).

Second, such an approach takes intervention under Rule 24 well beyond its proper context. As our discussion of *Marino* indicates (*supra* at 7-11), intervention is designed to permit *non-parties* to *litigate* an already-pending case under certain circumstances. Generally speaking, such non-parties do not have to be notified of the pendency of an action, and they are not bound by a judgment in that action. *Martin v. Wilks*, 490

U.S. at 762-65. Assuming that they do learn of the case, potential intervenors must file a motion to intervene, along with a "complaint in intervention," setting out the claims that they believe are not being adequately advanced by the named plaintiffs, or a defensive pleading "setting forth the ... defense for which intervention is sought." Fed. R. Civ. P. 24(c). The court then decides whether the non-party has a sufficient interest in the litigation to be granted party status. Fed. R. Civ. P. 24(a), (b).

In the class action settlement context, however, no one disputes that the absent class members *already* have legitimate interests in the litigation and that they will be bound by the class judgment. *See Matsushita*, 516 U.S. 367; *Shutts*, 472 U.S. at 812. Indeed, by definition, absent class members must hold the same claims as the named plaintiffs. *See General Telephone Co. of the Southwest v. Falcon*, 457 U.S. 147, 156 (1982); *see* Fed. R. Civ. P. 23(a)(2), (3). And it cannot seriously be argued that the class representatives who support the settlement adequately represent the interests of class members who oppose it. Here, for instance, the shareholders who instituted the suit on behalf of ADM support the settlement and as do their counsel, whose multi-million dollar fee hinges on its approval; on the other hand, the objecting shareholders maintain that the settlement, including its fees component, was a collusive "sell out" of the corporation's interests. *See* Petition at 5-7. Thus, because the adversity of interests between settlement supporters and settlement objectors is clear and irreparable, it makes no sense to put objectors through the Rule 24 process.

Third, and most important, imposing an "adequacy of representation" standard for intervention would bar effective appellate review of many class action settlements. Class actions are enormously useful tools for justice, because they provide

relief to large number of individuals who do not have the means to sue on their own. But class actions can be abused, largely because "the [class] lawyers might urge a class settlement at a low figure or on a less-than-optimal basis in exchange for red-carpet treatment for fees." *Weinberger v. Great Northern Nekoosa Corp.*, 925 F.2d 518, 524 (1st Cir. 1991). Although we take no position on the ultimate merit of the settlement before the Court, some of the facts—counsel's less-than-vigorous prosecution of the suit, the small monetary recovery, and counsel's gargantuan fee (Petition at 6-7)—raise considerable suspicion. In any event, the ever-present potential for collusion in itself favors an approach under which appellate review of class action settlements will remain robust.

Moreover, other dynamics of the settlement process in the district court counsel against any procedural hurdles that might frustrate appellate consideration of the merits. Once a class action settlement is reached, the district court's first action is usually to grant "preliminary approval," which is a finding that the settlement contains no obvious substantive or procedural defects. Manual § 30.41, at 237. After preliminary approval, the settling parties (usually the defendants) expend a considerable sum notifying the class of the settlement. Thereafter, the same district judge who preliminarily approved the settlement presides over a "fairness hearing" and decides whether to give final approval under Rule 23(e). *See id.* §§ 30.41-.42. Given the expense of mounting objections and the complexity of many settlements, the settlement may be viewed by class members as a "fait accompli." *Mars Steel Corp. v. Continental Ill. Nat'l Bank & Trust Co.*, 834 F.2d 677, 681 (7th Cir. 1987).

Not surprisingly, this process can create a hydraulic pressure for approval by the district courts, a view that is borne

out by the fact that the vast majority of settlements are approved without alteration. *See Empirical Study of Class Actions in Four Federal District Courts* 58 (Federal Judicial Center 1996) ("Approximately 90% or more of the proposed [class] settlements were approved without changes in each of the four districts"); *see generally* Koniak & Cohen, *Under Cloak of Settlement*, 82 U. Va. L. Rev. 1051, 1104-08 (1996) (recounting same phenomenon and describing motivations for district courts to approve class settlements). Under these circumstances, appellate review provides a critical bulwark against hastily approved, potentially unfair settlements. And if the settling parties are able to avoid an appeal on the merits by convincing the district judge that the objectors do not deserve to be intervenors, they may, in effect, give the district court the last word on settlement approval.

This Court's recent decision in *Amchem Products v. Windsor* was possible only because three small groups of objectors, 117 S. Ct. at 2241 n.7, had appealed the approval of the settlement to the Third Circuit, which conducted a comprehensive review of the merits. *See Georgine v. Amchem Prods., Inc.*, 83 F.3d 610 (3d Cir. 1996). *Amchem* not only set an important precedent on the applicability of Rule 23's certification criteria to settlement classes, 117 S. Ct. at 2248-49, but it overturned a settlement that had profoundly harmful effects on segments of the class whose interests had been sacrificed at the expense of those whom the settlement favored. *Id.* at 2250-52; *see generally* Koniak, *Feasting While The Widow Weeps: Georgine v. Amchem Products, Inc.*, 80 Cornell L. Rev. 1045 (1995). Other appellate decisions that have benefitted class members by rejecting unfair settlements and have contributed to the development of class action jurisprudence were possible only through the efforts of objecting class members. *See, e.g., General Motors*, 55 F.3d 768

(landmark decision regarding parameters of settlement class actions and attorney's fees).

In sum, an intervention requirement jeopardizes merits review of class action settlements. Although that outcome is championed by the court of appeals below in the name of efficiency, Pet. App. 4a-6a, *Felzen*, 134 F.3d at 874-75, such a rule would come at a very heavy price: frustration of rigorous appellate review, and thus greater potential for unfair and collusive class action settlements.

C. Requiring Intervention Is A Trap For Unwary Class Members.

Petitioners argue that, even if this Court agrees with respondents on the intervention issue, the ruling below was so drastic a departure from prior circuit law that it should be applied prospectively only. We agree with petitioners that retroactive application of the Seventh Circuit's ruling would be unfair, but, in our view, the debate over retroactive versus prospective application simply underscores the Seventh Circuit's error regarding intervention, which would impose a trap for unwary objeetors even after it were established law.

If this Court were to rule that intervention is required to appeal settlement approvals under both Rules 23 and 23.1, the likelihood that an objecting class member will neglect to seek intervention will diminish, but it will by no means evaporate. When a class action is settled, notice is sent out to class members who, in the main, are not represented by counsel. The notice informs the class members of the nature of the litigation, the terms of the settlement, and where and when they must file their objections. Manual, § 30.41, at 237. In short, at the settlement stage of modern class actions, thousands of litigants

are invited to participate on a *pro se* basis.

Even if we assume that a class member represented by counsel should know of the need to intervene, imposing that requirement on a *pro se* objector is at odds with reality. A layperson will not be aware of the niceties of federal procedure under Rule 24, and, thus, to condition the right to appeal on such knowledge would be illogical and unfair. To be sure, the standard class action notice could be amended to inform class members of the need to intervene to preserve their appellate rights, *see* Manual, § 41.43, at 488, but there is no reason to believe that non-lawyers would understand what intervention means or what a motion to intervene should contain. As long as a class member-objector files timely objections that focus the district court's attention on the settlement's alleged shortcomings, there is no basis for imposing an additional procedural requirement that jeopardizes the opportunity for appellate review on the merits for all objecting class members, especially for those who were not represented by counsel in the district court.

CONCLUSION

For the reasons stated above, the decision of the court of appeals should be reversed.

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IN THE
Supreme Court of the United States
OCTOBER TERM, 1998

CALIFORNIA PUBLIC EMPLOYEES' RETIREMENT SYSTEM, *et al.*,
Petitioners,

v.

PAUL FELZEN, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

BRIEF OF WASHINGTON LEGAL FOUNDATION AS *AMICUS CURIAE* IN SUPPORT OF RESPONDENTS

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QUESTION PRESENTED

Whether a nonparty shareholder who appears, in response to notice provided under Federal Rule of Civil Procedure 23.1, to present objections to a proposed dismissal or settlement of a derivative action may appeal an adverse decision even though the shareholder has not been formally made a party to the action.

TABLE OF CONTENTS

Page

QUESTION PRESENTED i

TABLE OF AUTHORITIES v

INTEREST OF AMICUS 1

STATEMENT OF THE CASE 2

SUMMARY OF ARGUMENT 7

ARGUMENT 9

I. GRANTING NONPARTY SHAREHOLDERS THE RIGHT TO APPEAL WITHOUT INTERVENING UNDERMINES THE PURPOSE OF DERIVATIVE ACTIONS 9

A. Shareholder Derivative Actions Serve the Purpose of Protecting Corporations from Economic Loss Caused by Faithless Fiduciaries 9

B. Derivative Actions Impose Significant Economic Losses on Corporations in the Form of Litigation Costs 12

C. Extending the Participation of Nonparty Shareholders by Creating a Right to Appeal Without Intervening Would Undermine the Purpose of Derivative Actions by Imposing Greater Litigation Costs on the Corporation ... 13

II. THIS COURT SHOULD DECLINE THE INVITATION TO CREATE A RIGHT TO APPEAL WHERE RULE 23.1 IS SILENT 16

A. Rule 23.1, Which Delimits the Extent of Nonparty Shareholders' Procedural Rights Regarding the Settlement of Derivative Actions, Nowhere Confers the Right of Appeal Sought by Petitioners 16

B. Petitioners' Policy Arguments Amount to An Invitation to Rewrite Rule 23 17

C. Rule 23.1 Provides Adequate Protection Against Unfair or Collusive Settlements in Derivative Actions 23

D. If Rule 23.1 Requires Amending, this Court Ought to Leave the Task to the Rulemaking Procedure that Congress Has Prescribed 24

CONCLUSION 27

TABLE OF AUTHORITIES

Cases: Page

Alleghany Corp. v. Kirby,
333 F.2d 327 (2d Cir. 327) 19
Amchem Prods., Inc. v. Windsor,
117 S. Ct. 2231 (1997) 25
Armstrong v. Board of Sch. Dir.,
616 F.2d 305 (7th Cir. 1979) 24
Bell Atl. Corp. v. Bolger,
2 F.3d 1304 (3rd Cir. 1993) 7
Birnbaum v. Birrell,
17 F.R.D. 409 (S.D.N.Y. 1955) 23, 24
Burks v. Lasker, 441 U.S. 471 (1979) 18
Cohen v. Beneficial Loan Corp.,
337 U.S. 541 (1949) 9
Daubert v. Merrell Dow Pharm., Inc.,
509 U.S. 579 (1993) 1
Granada Invest., Inc. v. DWG Corp.,
962 F.2d 1203 (6th Cir. 1992) 13
In re Brand Name Prescription Drugs Antitrust Litig.,
115 F.3d 456 (7th Cir. 1997) 5
In re Pacific Enterprises Secs. Litig.,
47 F.3d 373 (9th Cir. 1995) 13, 19
Kamen v. Kemper Fin. Services, Inc.,
500 U.S. 90 (1991) 9
Kearney v. Jandernoa,
934 F. Supp. 863 (W.D. Mich. 1996) 12
Koster v. Lumbermen's Mut. Cas. Co.,
330 U.S. 518 (1947) 11
Marino v. Ortiz,
484 U.S. 301 (1988) ..... *passim*
Matsushita Elec. Indus. Co. v. Epstein,
116 S. Ct. 873 (1996) 1
McDermott v. Amclyde & River Don Castings Ltd.,
511 U.S. 202 (1994) 24
Omni Capital Int'l v. Rudolf Wolff & Co.,
484 U.S. 97 (1987) 25

Papilsky v. Berndt,
466 F.2d 251 (2nd Cir. 1972) 10
Pavelic & LeFlore v. Marvel Entertainment Group,
493 U.S. 120 (1989) 17
Rosenbaum v. MacAllister,
64 F.3d 1439 (10th Cir. 1995) 19
Smith v. Sperling,
354 U.S. 91 (1957) 10–11
Tryforos v. Icarian Dev. Co.,
518 F.2d 1258 (7th Cir. 1975) 6–7

Statutes and Rules:

28 U.S.C. § 2072 (1998) 25
Fed. R. App. P.3(c) 6
Fed. R. Civ. P. 1 16
Fed. R. Civ. P. 23.1 ..... *passim*
S. Ct. R. 37.1 1

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Greg Burns, *A Grain of Activism at Archer Daniels Midland*, Bus. Wk., Nov. 6, 1995 2
John A. Byrne, *The Best and the Worst Boards*, Bus. Wk., Nov. 25, 1996 2
WILLIAM L. CARY & MELVIN A. EISENBERG, CORPORATIONS (1988) 19
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Reinier Kraakman *et al.*, *When Are Shareholder Suits in Shareholder Interests?*, 82 GEO. L.J. 1733 (1994) 7, 9, 13
Levi & Moore, *Federal Intervention: II. The Procedure, Status, and Federal Jurisdictional Requirements*, 47 YALE L.J. 898 (1938) 17
Roger Lowenstein, *Corporate Governance's Sorry History*, Wall St. J., Apr. 19, 1996 2
J. MOORE, MOORE'S FEDERAL PRACTICE (D. Coquillette, *et. al.* eds., 3rd ed. 1998) 18, 23
J. Moore & M. Cohn, *Federal Class Actions—Jurisdiction and Effect of Judgment*, 32 ILL. L. REV. 555, 556 (1938). 18
Order, 507 U.S. 1091 (1993) 26
Carol B. Swanson, *Corporate Governance: Sliding Seamlessly into the Twenty-first Century*, 21 J. CORP. LAW 417 (1996) 7
Ralph K. Winter, *Paying Lawyers, Empowering Prosecutors, and Protecting Managers: Raising the Cost of Capital in America*, 42 DUKE L.J. 945 (1993) 12

INTEREST OF *AMICUS CURIAE*

The Washington Legal Foundation (WLF) is a nonprofit public interest law and policy center based in Washington, D.C., with supporters across the nation.[1] WLF regularly appears in legal proceedings before federal and state courts, as well as administrative bodies, to defend the principles of free enterprise and limited government.

WLF has devoted substantial resources to promote civil justice reform. Through litigation and publishing it has endeavored to prevent excessive litigation from impeding this nation's economic growth. To that end, WLF has appeared before this Court and other federal and state courts in several cases. *See, e.g.*, *Matsushita Electric Industrial Co. v. Epstein*, 116 S. Ct. 873 (1996) (the proper scope of class action litigation); *Daubert v. Merrell Dow Pharmaceuticals, Inc.*, 509 U.S. 579 (1993) (use of expert scientific evidence in litigation).

WLF is filing the attached brief because of its ongoing interest in promoting the welfare of the business community and the public at large. It has no direct economic interest in the outcome of this lawsuit or in other suits raising similar issues. For that reason, WLF believes that it can assist the Court by supplying a disinterested perspective that is distinct from that of any party. All parties have consented to the filing of this brief, and their letters of consent have been lodged with the Clerk of the Court.

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[1] Pursuant to Supreme Court Rule 37.6, the Washington Legal Foundation states that no counsel for a party authored this brief in whole or in part; and that no person or entity, other than the Washington Legal Foundation and its counsel, contributed monetarily to the preparation and submission of this brief.

STATEMENT OF THE CASE

In the interests of brevity, WLF hereby incorporates by reference the Statement of the Case contained in the Brief for Respondents.

This case arose when Archer Daniels Midland Company (ADM) suffered financial losses brought on by two causes.

First, ADM suffered severe financial losses when it became the target of a federal criminal investigation. On October 15, 1996, ADM pleaded guilty to criminal antitrust charges for conspiring with rivals to fix prices for citric acid, high fructose corn syrup, and lysine. As a penalty, the court imposed on ADM the largest criminal antitrust fine in history: $100 million. And this price tag, while enormous, described only part of ADM's burden. ADM paid out another $90 million to settle three civil antitrust actions, which its competitors brought as a direct result of the criminal probe.

Second, ADM suffered losses from alleged mismanagement. Journalists, industry analysts, and a major shareholder publicly criticized ADM for maintaining allegedly overly close ties between management and members of the board, whose duties included overseeing management. *See, e.g.*, John A. Byrne, *The Best and the Worst Boards*, Bus. Wk., Nov. 25, 1996; Roger Lowenstein, *Corporate Governance's Sorry History*, Wall St. J., Apr. 19, 1996, at C2; Martha Irvine, *Guilty Verdict May Change Plans for Top Management at Agribusiness*, Assoc. Press, Sept. 20, 1998; Greg Burns, *A Grain of Activism at Archer Daniels Midland*, Bus. Wk., Nov. 6, 1995, at 44.

ADM responded to these criticisms and to its antitrust troubles by commissioning a report proposing reforms to ADM's corporate governance. Adopted in January 1996, these reforms required the board to include a majority of independent members. But adopting the report did not put an end to the criticism of ADM. Major ADM shareholders, including Petitioners California Public Employees' Retirement System (CalPERS) and the Florida State Board of Administration (SBA), unsuccessfully challenged the proposed reforms.

As a result of the criminal probe and the public criticisms of ADM's governance practices, several shareholder derivative actions were filed on behalf of ADM. These were consolidated by May 1996 in the United States District Court for the Central District of Illinois. The consolidated action accused ADM's directors of "gross mismanagement" Br. Pet. at 5, for failing to properly supervise corporate employees. Plaintiffs sought to recover the $190 million ADM had been obligated to pay in criminal fines and civil settlements because of the antitrust conviction.

On May 29, 1997, plaintiffs' counsel and the insurance company covering ADM and its board members arrived at a settlement. It required the defendants to pay $8 million in exchange for a release of "any and all causes of action" against the defendants. The parties agreed that the entire amount would be allocated for attorneys fees. Roughly half was to be paid to plaintiffs' counsel, and the other half was to be reserved for ADM's future legal expenses, incurred as a consequence of carrying out the corporate reforms described in the settlement. These reforms included a restructuring of the board and procedures to enhance director independence. Professor John C. Coffee, Jr.,

who was "retained by the plaintiffs' attorneys to apprise the adequacy and significance of the corporate governance provisions," Joint App. at 225, contained in the settlement, characterized the reforms as "more or less the 'state of the art' in American corporate governance today." Joint App. at 226.

After executing this settlement, the parties and defendants filed a written motion seeking approval of the settlement from the district court. On May 30, 1997, the court issued an Order Preliminarily Approving Settlement and Providing for Notice. The order directed the parties to give all ADM shareholders written notice of the proposed settlement. Along with that notice came an order to show cause, offering nonparty shareholders an opportunity to present objections to the settlement.

On July 7, 1997, the district court approved the settlement and entered judgment accordingly. CalPERS and SBA filed a timely notice of appeal to the United States Court of Appeals for the Seventh Circuit, but they did not intervene in the action.

Some Respondents filed a motion in the United States Court of Appeals for the Seventh Circuit, seeking dismissal of the appeal. They argued that CalPERS and SBA could not appeal from the district court's judgment approving the settlement, because they had not intervened as parties. The court agreed.

The Seventh Circuit dismissed the Respondents' appeal for want of jurisdiction. *See* Pet. App. at 10a. Judge Easterbrook, writing for a unanimous panel that also included Chief Judge Posner and Judge Flaum, decided that shareholders who have been summoned to present objections to a proposed settlement in a

derivative action must intervene if they wish to appeal an adverse decision. *See id.* at 2a, 7a.

The Seventh Circuit's analysis primarily relied on a statement this Court made in *Marino v. Ortiz*, 484 U.S. 301 (1988): "The rule that only parties to a lawsuit, or those that properly become parties, may appeal an adverse judgment, is well settled." *Id.* at 304 (citations omitted). Although this statement from *Marino* arose out of an appeal from a consent decree in a class action, the appeals court pointed out that it had already expanded the application of *Marino* beyond that narrow context. In *In re Brand Name Prescription Drugs Antitrust Litigation*, 115 F.3d 456 (7th Cir. 1997), it held that an unnamed member of a class in a class action may not appeal from a summary judgment order granted in favor of a defendant. For that reason, the Seventh Circuit couched the issue in this case in terms of whether objecting nonparty shareholders in a derivative action deserved what unnamed class members in a class action did not deserve, namely, treatment as an exception to the "only parties may appeal" rule of *Marino*. For several reasons, the panel concluded that such shareholders did not merit an exception to *Marino*.

First, the Seventh Circuit cited fidelity to this Court's precedent as a reason not to carve out an exception to *Marino*. There this Court explained that "the better practice," 484 U.S. 301, 304 (1988), when a nonparty has a legal interest that a district court decision will affect, is to "seek intervention for purposes of appeal." *Id.* On this basis, the Seventh Circuit interpreted *Marino* to mean that federal circuit courts lack the authority to make exceptions to the rule that "only parties may appeal adverse judgments." *See* Pet. App. at 3a.

Second, the lower court cited Rule 3(c) of the Federal Rules of Appellate Procedure in support of *Marino*. If "[a] notice of appeal must specify the party or parties taking the appeal," *Id.*, the court reasoned, then only parties may appeal. *See* Pet. App. at 2a.

Third, the Seventh Circuit rejected the argument that because "erroneous decisions should be reversed," Pet. App. at 3a, intervention is unnecessary. As the court emphasized, "A court of appeals is not an ombudsman." *Id.* Erroneous district court judgments "do not justify omitting the step of intervening as a party." *Id.*

Finally, the Seventh Circuit panel rejected the argument that the distinction between nonparty shareholders in a derivative suit and unnamed plaintiffs in a class action justifies a right of appeal for the former if not the latter. As the panel keenly observed, such a distinction "cut[s] against," Pet. App. at 4a, the nonparty shareholders' position. "[E]ach class member has a real grievance with the defendant that sets up at least an equitable argument for a class member who wants to appal. But in a shareholders' derivative action, the individual investor is not an injured party and is not entitled to litigate. . . ." *Id.* at 4a-6a (citations omitted).

The circuit panel acknowledged that its own pre-*Marino* precedent had allowed nonparty shareholders in a derivative action to appeal without intervening. *See Tryforos v. Icarian Development Co.*, 518 F.2d 1258, 1263 n.22 (7th Cir. 1975). However, the court decided to overrule *Tryforos*. In its judgment, not only did *Tryforos* fail to explain why nonparty shareholders possess the right to appeal without intervening, but

it predated this Court's pronouncement in *Marino*. *See* Pet. App. at 3a.

The court below also recognized that its reasoning put it at odds with the Third Circuit's decision in *Bell Atlantic Corp. v. Bolger*, 2 F.3d 1304 (3rd Cir. 1993). There the court held that a shareholder need not intervene to appeal from a district court's decision to accept settlement of a derivative action. *See id.* at 1307-10. The Third Circuit reached this conclusion on the ground that shareholders have standing. The Seventh Circuit disagreed. It argued that *Marino* requires circuit courts to treat a shareholder's status as a party or nonparty, not the injury it can show, as dispositive in determining whether a particular shareholder may appeal from an adverse decision in the district court. "Equating injury with party status is exactly the approach disapproved by *Marino*." Pet. App. at 7a.

SUMMARY OF ARGUMENT

Shareholder derivative actions play an important role in the American economy. According to some commentators, they serve as "the primary mechanism for enforcing the fiduciary duties of corporate managers." Reinier Kraakman *et al.*, *When Are Shareholder Suits in Shareholder Interests?*, 82 GEO. L.J. 1733, 1733 (1994). At the same time, however, "shareholder derivative suits have been controversial since their inception." Carol B. Swanson, *Corporate Governance: Sliding Seamlessly into the Twenty-first Century*, 21 J. CORP. LAW 417, 437 (1996).

The Question Presented requires this Court to decide whether shareholder derivative litigation shall be conducted according to the Federal Rules of Civil Procedure, or not. The Seventh Circuit held that since

"only parties to a lawsuit, or those that properly become parties, may appeal an adverse judgment," *Marino v. Ortiz*, 484 U.S. 301, 304 (1988), nonparty shareholders may not, by definition, appeal from a district court decision accepting a proposed settlement of the consolidated derivative action brought against ADM's directors and officers. *See* Pet. App. at 2a, 7a. That decision finds strong support in both policy and law.

From the viewpoint of policy, granting nonparty shareholders a right of appeal to contest adverse settlement decisions undermines the purpose of derivative actions. Derivative actions were designed to permit shareholders to bring an action to prevent a corporation from being economically destroyed by faithless fiduciaries. Their useful purpose is undermined, however, if derivative actions are permitted to be extended too far. Derivative actions, as with any species of litigation, impose large costs on corporations. Deciding how extensively nonparty shareholders may participate in derivative actions is a potentially ticklish question, which has fortunately been decided by those who drafted and enacted Rule 23.1.

Rule 23.1 nowhere contains a right of appeal for nonparty shareholders wishing to contest a district court's decision to approve the settlement of a derivative action. For various policy reasons, Petitioners and their *amici* invite this Court to create one where the drafters of Rule 23.1 saw fit not to. Such judicial creativity is unnecessary because the rule provides adequate protection against the same evils, namely, unfair or collusive settlements, which Petitioners' newly-minted right of appeal would supposedly provide. In addition, declining Petitioners' invitation would be in keeping with this Court's oft-stated commitment

to eschew judicial legislation when construing the Federal Rules of Civil Procedure. If Petitioners and their *amici* are correct in arguing that Rule 23.1 needs to include a right of appeal for nonparty objecting shareholders, then amendment ought to be left to the rulemaking procedure prescribed by Congress.

ARGUMENT

I. GRANTING NONPARTY SHAREHOLDERS THE RIGHT TO APPEAL WITHOUT INTERVENING UNDERMINES THE PURPOSE OF DERIVATIVE ACTIONS.

A. Shareholder Derivative Actions Serve the Purpose of Protecting Corporations from Economic Loss Caused by Faithless Fiduciaries.

"Devised as a suit in equity, the purpose of the derivative action was to place in the hands of the individual shareholder a means to protect the interests of the corporation from the misfeasance and malfeasance of 'faithless directors and managers.'" *Kamen v. Kemper Financial Services, Inc.*, 500 U.S. 90, 95 (1991) (quoting *Cohen v. Beneficial Loan Corp.*, 337 U.S. 541, 548 (1949)). "Such suits often allege that an officer or director has breached his duty of loyalty; in other words, that the manager has effectively 'cheated' the company by self-dealing, accepting kickbacks, appropriating a corporate opportunity, wasting corporate assets, or entrenching his position to avoid removal." Reinier Kraakman *et al.*, *When Are Shareholder Suits in Shareholder Interests?*, 82 GEO. L.J. 1733, 1733 (1994) (footnote omitted). The narrow range of legal interests protected by derivative actions is sometimes misunderstood.

CalPERS and SBA complain that under the terms of the proposed settlement, "Not one dime [would be] returned to the corporation for the benefit of shareholders who lost at least $190 million in value as a result of their fiduciaries' misconduct." Br. Pet. at 7. In its brief supporting CalPERS and SBA, the United States claims that a nonparty objecting shareholder in a derivative action has personal legal rights at stake in the action. "Rule 23.1 protects absent shareholders from settlements that unfairly compromise their interests by providing them with notice and an opportunity to object to settlements and by requiring court approval of settlements." Br. United States & SEC As *Amici Curiae* Supp. Pets. [*hereinafter* Br. U.S.] at 19; *see also id.* at 16 ("Rule 23.1 specifically recognizes the shareholder's personal rights . . . ."); *Id.* at 18 ("[T]he objecting shareholder has a personal stake in the outcome of a derivative action settlement."). These assertions of shareholder interests in the face of multimillion-dollar corporate losses are entirely understandable. However, they have led Petitioners and their *amici* to misunderstand the nature of derivative actions.

Derivative actions protect the corporation from the economic injuries caused by disloyal fiduciaries. Such injuries take many forms, including the criminal penalties, civil settlement costs, and loss of shareholder confidence at issue in this case. *See* Br. Pet. at 2-4. These injuries will likely cause the value of a corporation's shares to fall. But derivative actions are not designed to remedy a shareholder's personal financial loss in such circumstances. *Papilsky v. Berndt*, 466 F.2d 251 (2nd Cir. 1972). As Justice Frankfurter long ago emphasized, "The contrasting difference between a stockholder's suit for his corporation and a suit by him against it, is crucial." *Smith v. Sperling*,

354 U.S. 91, 99 (1957) (Frankfurter, J., dissenting). His explanation of the distinction, though somewhat lengthy, is worthwhile for its clarity:

> In the former, [the stockholder] has no claim of his own; he merely has a personal controversy with his corporation regarding the business wisdom or legal basis for the latter's assertion of a claim against third parties. Whatever money or property is to be recovered would go to the corporation, not a fraction of it to the stockholder. When such a suit is entertained, the stockholder is in effect allowed to conscript the corporation as a complainant on a claim that the corporation, in the exercise of what it asserts to be its uncoerced discretion, is unwilling to initiate. This is a wholly different situation from that which arises when the corporation is charged with invasion of the stockholder's independent right. Thus, for instance, if a corporation rearranges the relationship of different classes of security holders to the detriment of one class, a stockholder in the disadvantaged class may proceed against the corporation as a defendant to protect his own legal interest.

Id.; *see also Koster v. Lumbermen's Mut. Cas. Co.*, 330 U.S. 518, 522 (1947) (comparing derivative actions with suits brought on behalf of a "next friend" when the real party in interest cannot protect itself).

Derivative actions serve a legitimate purpose by protecting the corporation from the economic damage inflicted by faithless fiduciaries. Such actions protect the interests of a corporation, considered apart from the interests of shareholders, directors, and officers.

For that reason, it is inaccurate for Petitioners and their *amici* to speak of "shareholders' interests" in the context of a derivative action. As the name suggests, such an action *derives* from the interests of the corporation. *See Kearney v. Jandernoa*, 934 F. Supp. 863, 867 (W.D. Mich. 1996). And it is those interests, not the interests of shareholders, which ought to govern in any discussion of the policies underlying the procedures by which derivative actions are maintained in the federal courts.

B. Derivative Actions Impose Significant Economic Losses on Corporations in the Form of Litigation Costs.

In permitting shareholders to protect a corporation's interest by bringing an action against delinquent fiduciaries, derivative actions serve a useful, indeed at times essential, purpose. But derivative actions, like any other kind of litigation, cost substantial amounts of time and money. A balanced appraisal of the right to appeal sought by CalPERS and SBA must take account of that fact.

To evaluate the cost of derivative actions to a corporation, one must start with the fact that "plaintiffs [in derivative and class actions] are generally figureheads .... because the real incentive for bringing such actions is the quest for attorney's fees." Ralph K. Winter, *Paying Lawyers, Empowering Prosecutors, and Protecting Managers: Raising the Cost of Capital in America*, 42 DUKE L.J. 945, 948 (1993). Because attorneys fees lie at the heart of how derivative suits are conducted, they account for a large portion of any settlement recovered on behalf of the corporation. *Cf.* J. Alexander, *Do the Merits Matter? A Study of Settlements in Securities Class Actions*, 43 STAN. L. REV.

497, 573 (1991) (suggesting that for every dollar awarded to shareholders in securities law class actions, another dollar goes toward litigation costs).

That derivative litigation is largely driven by the "quest" for attorneys fees largely accounts for its high cost to corporations. *See* Reinier Kraakman *et al.*, *When Are Shareholder Suits in Shareholder Interests?*, 82 GEO. L.J. 1733, 1738 n.15 (1994). *see also* A.F. Conard, *Winnowing Derivative Suits Through Attorneys Fees*, 47 LAW & CONTEMP. PROBS. 269, 281-82 (1984) (noting that multimillion dollar derivative suits, coupled with the contingency fees customary in such suits, "inspire [the] filing [of] some long-shot lawsuits."). Multimillion dollar attorneys fee awards are not uncommon in these cases. *See, e.g., In re Pacific Enterprises Secs. Litig.*, 47 F.3d 373, 376 (9th Cir. 1995) (awarding $4 million in attorneys fees); *Granada Investments, Inc. v. DWG Corp.*, 962 F.2d 1203, 1207 (6th Cir. 1992) (awarding $4.1 million in attorneys fees).

Not all the high cost of derivative litigation can be measured in dollars, however. Some of the cost comes in the form of "time and energy." 82 GEO. L.J. 1733, 1738 (1994). Other indirect costs include "loss of morale, deflection of employee time, and injury to the corporate reputation." James D. Cox, *Searching for the Corporation's Voice in Derivative Suit Litigation*, 1982 DUKE L.J. 959, 960.

C. Extending the Particiation of Nonparty Shareholders by Creating a Right to Appeal Without Intervening Would Undermine the Purpose of Derivative Actions by Imposing Greater Litigation Costs on the Corporation.

Granting nonparty shareholders the right to appeal sought by CalPERS and SBA extends the life of a derivative action by delaying a settlement that would otherwise bring that action to an end. And extending the action increases litigation costs. Thus, at some point, granting nonparty shareholders a right to appeal without intervening from a decision to accept a settlement in a derivative action threatens to undermine the purpose of derivative actions themselves.

Writing in support of CalPERS and SBA, the Council of Institutional Investors asserts that corporations receive financial benefits from the improvements that nonparty objecting shareholders brings to the settlement hearing. *See* Brief of *Amicus Curiae* Council of Institutional Investors in Support of Petitioners [*hereinafter* Br. Council] at 15-16. Their analysis appears to assume that reducing the portion of the settlement devoted to attorneys fees necessarily benefits the corporation. On this point they are mistaken.

As some commentators have observed, even a legitimate derivative action may not yield a net financial gain to the corporation.

> The litigation costs imposed on the firm may well exceed the damages awarded even in successful suits. Some derivative suits are based on public policy issues and, if won, clearly will reduce stockholder wealth. For example, suits motivated by environmental concerns or brought to halt the payment of bribes to foreign officials would, if successful, undoubtedly decrease the wealth of the firm's equity holders. Finally, some argue that the derivative suit is designed primarily to enhance the welfare of the plaintiffs,

> or the plaintiffs' counsel, and not the welfare of the firm's equityholders in general. Based on these considerations, the termination of a derivative suit might well increase the price of the firm's equity, and a continuance might decrease its market price.

Daniel R. Fischel & Michael Bradley, *The Role of Liability Rules and the Derivative Suit in Corporate Law: a Theoretical and Empirical Anaylsis*, 71 CORNELL L. REV. 261, 279 (1986).

Early settlement, even of frivolous claims, may often cost the corporation less than continuing to litigate. *See* Joseph A. Grundfest, *Why Disimply?*, 108 HARV. L. REV. 727, 742-43 (1995) (suggesting that settlement values often fall below avoided litigation costs). Conversely, delaying settlement needlessly, as Petitioners' automatic right of appeal for nonparty shareholders would permit, will impose unnecessarily high litigation costs on the corporation whose interest the derivative action was intended to protect.

The corporation, considered apart from its shareholders, directors, and officers, thus finds itself in a vise. On the one side it feels the economic pinch from fiduciaries, whose disloyalty can inflict potentially life-threatening economic damage. From the other side it feels the pinch of litigation costs. Viewed from a policy perspective, deciding how extensively nonparty shareholders may participate in derivative actions raises a potentially ticklish question of competing values. Fortunately the question has been resolved by those who drafted and enacted Rule 23.1.

II. THIS COURT SHOULD DECLINE THE INVITATION TO CREATE A RIGHT TO APPEAL WHERE RULE 23.1 IS SILENT.

A. Rule 23.1, Which Delimits the Extent of Nonparty Shareholders' Procedural Rights Regarding the Settlement of Derivative Actions, Nowhere Confers the Right of Appeal Sought by Petitioners.

Rule 23.1 of the Federal Rules of Civil Procedure (FRCP) provides in relevant part as follows:

> The derivative action may not be maintained if it appears that the plaintiff does not fairly and adequately represent the interest of the shareholders or members similarly situated in enforcing the right of the corporation or association. The action shall not be dismissed or compromised without the approval of the court, and notice of the proposed dismissal or compromise shall be given to shareholders or members in such manner as the court directs.

Two preliminaries regarding Rule 23.1 are worth noting.

First, as one of the Federal Rules of Civil Procedure (FRCP), Rule 23.1 "govern[s] the procedure in the United States district courts in all suits of a civil nature." FRCP 1. That is, Rule 23.1 governs the procedure to be followed in derivative actions brought in federal district court.

Second, as with all of the FRCP, Rule 23.1 must be "construed and administered to secure the just, speedy, and inexpensive determination of every action." FRCP 1. To accomplish these ends, the Court has

declared that it "give[s] the Federal Rules of Civil Procedure their plain meaning." *Pavelic & LeFlore v. Marvel Entertainment Group*, 493 U.S. 120, 123 (1989).

The plain meaning of Rule 23.1 nowhere contains the right of appeal so urgently sought by CalPERS and SBA. Nothing in the plain language of Rule 23.1 confers on objecting shareholders an appeal as of right. The only procedural right expressly conferred on nonparty shareholders by the rule is a right to notice of any "proposed dismissal or compromise." *Id.*

Along with this right of notice comes the opportunity for a judicial hearing. However, as the drafters of the original version of FRCP cogently observed, "It must be remembered that the right to be heard is not the same as intervention . . . . One who is only given a right to be heard, and has not intervened, has no right of appeal." Levi & Moore, *Federal Intervention: II. The Procedure, Status, and Federal Jurisdictional Requirements*, 47 YALE L.J. 898, 938 (1938).

B. Petitioners' Policy Arguments Amount to An Invitation to Rewrite Rule 23.1.

CalPERS and SBA, along with their supporting *amici*, raise several policy arguments that, in essence, amount to an invitation for this Court to look beyond the plain language of Rule 23.1. Their reasons for asking this Court to invent a right of appeal where the rule is silent can be organized under the following headings:[2]

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[2] The statements contained in the headings appear to be representative of positions held by Petitioners and their *amici* collectively, since no argument to which the headings refer is exclusively raised in a single brief. In fairness, however, we point out that not every statement made in a heading appears in every

(continued...)

1. Only objecting nonparty shareholders can prevent unfair or collusive settlements in derivative actions.

CalPERS, SBA, and their supporting *amici* place great weight on the importance assigned by Rule 23.1 to objecting nonparty shareholders. "Objecting shareholders play a critical role in ensuring the fairness of derivative suit settlements." Br. Pet. at 32; Brief for the United States and the Securities and Exchange Commission as *Amici Curiae* Supporting Petitioners [*hereinafter* Br. U.S.] at 22 ("The objecting shareholders play a pivotal role in the settlement approval process . . . .").

Petitioners and their *amici* next point out that derivative actions carry the "risk that the representative plaintiff will collude with the defendant to forgo the derivative claims in exchange for a settlement that is only favorable to the representative plaintiff and his or her attorneys." 5 *Moore's Federal Practice* § 23.1.10[2][a], at 23.1-58 (1998); *see also Burks v. Lasker*, 441 U.S. 471, 485 n.16 (1979) (Rule 23.1's notice requirement is intended "to prevent plaintiffs from selling out their fellow shareholders."); J. Moore & M. Cohn, *Federal Class Actions—Jurisdiction and Effect of Judgment*, 32 ILL. L. REV. 555, 556 (1938). ("[N]otice [to nonparty shareholders] will tend to lessen strike suits by shareholders, since a shareholder and his counsel will not be able to sue and settle in the dark; and it will prevent unrighteous com promise of a just shareholders' action.").

From these premises Petitioners and their *amici* conclude, "*Only* objecting shareholders can give a

[2] (...continued)
brief.

federal court the benefit of an adversarial presentation as to whether a particular settlement is 'fair and adequate' and thus should be approved." Pet. Br. at 32 (emphasis added); Br. U.S. at 22-23 ("The objecting shareholders play a pivotal role in the settlement approval process, since they *alone* have the incentive to attempt to stop a process that builds momentum from the moment a deal is struck between the derivative plaintiff and the defendant.") (emphasis added).

In addition, Petitioners and their *amici* argue that "the efforts of non-party shareholder objectors in a wide variety of cases have resulted 'in significant improvement of the settlement.'" Br. Council at 15 (quoting WILLIAM L. CARY & MELVIN A. EISENBERG, CORPORATIONS 1057 (1988)). In support of this claim, they point to cases where objecting shareholders successfully obtained either increases in the settlement amount or reductions in the attorneys fees contained in the settlement. *See id.* (citing *In re Pacific Enters. Sec. Litig*, 47 F.3d 373, 375, 377 (9th Cir. 1995); *Alleghany Corp. v. Kirby*, 333 F.2d 327, 331-32 (2d Cir. 327); *Rosenbaum v. MacAllister*, 64 F.3d 1439, 1447-48 (10th Cir. 1995)); *see also* Br. Pet. at 33.

In effect, these statements by CalPERS, SBA, and their *amici* amount to the claim that nonparty objecting shareholders must have the right to appeal, or unfair and collusive settlements will be approved otherwise.

2. Requiring nonparty objecting shareholders to intervene in order to appeal would harm the corporation by reducing the number of objecting shareholders who contest derivative action settlements.

CalPERS and SBA next argue that "[r]equiring intervention as a prerequisite for such appeals would dramatically decrease [the number of objecting shareholders] and thereby impair the ability of objecting shareholders to serve the recognized public function of exposing, defeating, and deterring collusive or inadequate settlements." Pet. Br. at 33; *see also* Br. Council at 24 n.14 ("Even small increases in costs imposed on the monitoring function will have a substantial effect on the incentive and ability of shareholders to restrain unfair settlements."). They justify this conclusion by citing "the legal hurdles to intervention by objecting shareholders at the settlement phase," Pet. Br. at 34, and the "enormous practical disincentives." Pet. Br. at 35. Legal obstacles include the difficulty of intervening late in the proceedings, when settlement has been proposed, as well as the contemporaneous ownership rule, Br. Council at 22, which limits potential parties in a derivative suit to those who were shareholders "at the time of the transaction of which the plaintiff complains." Rule 23.1. Practical disincentives include "short notice periods," Brief of Barclays Global Investors, N.A., et al., As Amici Curiae Supporting Petitioners [*hereinafter* Br. Barclays] at 11, "lengthy procedures for making a decision to intervene," *Id.*, "small legal budgets and small legal staffs," *Id.* at 13, and the "burdens and costs associated with intervention." *Id.* at 15; *see* Br. Council at 23 ("the costs of intervention are substantial.").

This argument looks like the first, only in reverse. There the argument was that the capacity of objecting shareholders to prevent the imposition of unfair or collusive settlements justifies the creation of a right of appeal where Rule 23.1 is silent. Here Petitioners and their *amici* argue, in effect, that a judicially-created right of appeal is justified because objecting

shareholders will be prevented from challenging (supposedly) troubling settlements otherwise.

3. *Appellate review tends to render unfair or collusive settlements less likely by reversing and deterring erroneous district court settlement approvals and by rendering district courts more cautious in evaluating the objections to a settlement brought forward by nonparty shareholders.*

CalPERS, SBA, and their *amici* argue that appellate review is necessary to check the overhastiness or ignorance of district courts. "Appellate review is an essential component of shareholder participation because it provides a strong incentive for district courts to consider shareholder objections fully and a direct avenue for correcting district court errors." Pet. Br. at 33 (citations omitted).; *see also* Br. Council at 18 ("appellate review is critical to ensuring the fairness of shareholder derivative settlements"). The Council cites "correction of error," at 17, as "a powerful incentive for the district court to render more careful findings of fact and to develop a better record," *Id.*, as reasons why appellate review of derivative action settlements is desirable. "The availability of appeal also causes trial courts to consider the objections of shareholders more carefully in the first instance." Br. Council at 19.

Appellate review carries undoubted advantages. However, the arguments of Petitioners and their *amici* add up to something more negative than a natural desire to have another bite at the apple. They appear to betoken suspicion, if not outright mistrust, of district courts.

Strong arguments in favor of appellate review often come with a correspondingly strong suspicion (at times bordering on mistrust) against the sufficiency of district court judgments. That is true in this case. "The opportunity to challenge settlements of those private disputes in the district court without the corresponding right to appeal is not sufficient when there is a natural tendency among trial courts to favor approving settlements to which the named parties have agreed." Br. U.S. at 23. Appellate review will ensure "the opportunity for appellate scrutiny of what otherwise would be largely unreviewable proceedings." *Id.* at 24. The Council of Institutional Investors makes this point with particular force. Although Rule 23.1 imposes on district courts the duty to evaluate whether a proposed settlement serves the interests of the corporation, the Council opines that "a district court may be poorly situated to fulfill this duty on its own." Br. Council at 12. The Council cites two reasons for suspecting the capacity of district courts, neither of which casts them in a flattering light. "[I]n considering a settlement proposal, a district court may have relatively limited knowledge of the underlying action" *Id.* at 12-13. "[T]here is a strong institutional bias in favor of settlement" *Id.* at 13.

All of these arguments in favor of appellate review can be interpreted in two ways. They can be read to mean that the virtues of appellate review, including error correction, deterrence of future error, and promoting greater sensitivity of district courts toward nonparty shareholders during the settlement hearing, justify the Court in finding a right to appeal that the plain language of Rule 23.1 does not contain. Or the arguments can read to mean that suspicion (or mistrust) of district courts and their capacity (or willingness) to smoke out and reject unfair or collusive settlements

justifies the creation of a right of appeal for objecting shareholders. Either way calls for the Court to rewrite Rule 23.1 to include a right of appeal on which the rule as written is silent.

C. Rule 23.1 Provides Adequate Protection Against Unfair or Collusive Settlements in Derivative Actions.

Despite the various fears expressed by Petitioners and their *amici*, Rule 23.1 adequately protects corporations against unfair or collusive settlements in derivative actions. Such protection includes the requirement of judicial approval before any derivative action may be "dismissed or compromised," FRCP 23.1, and notice to every shareholder of the proposed settlement. *See id.* The drafters of the rule erected these safeguards against the collusive and unfair settlements so frequently cited by CalPERS, SBA, and their *amici* as a cause for concern. *See, e.g., Birnbaum v. Birrell*, 17 F.R.D. 409, 411 (S.D.N.Y. 1955).

In addition, objecting nonparty shareholders hold significant rights, even without the right of appeal sought by Petitioners. They "must be allowed to have meaningful participation at a settlement hearing," including "certain rights to discovery and cross-examination on issues pertaining to the settlement." 5 *Moore's Federal Practice* at § 23.1.10[1][c].

These procedural protections are adequate, if not perfect. It may be true that another level of judicial scrutiny would improve, even substantially improve, the quality of settlements in derivative suits. But the those who drafted and enacted the rules did so with an apparent intent to accommodate competing interests.

Derivative actions primarily serve the interests of corporations, who often benefit from early and inexpensive settlement. Corporations' interest in achieving settlements is favored by the law. *See, e.g., McDermott v. Amclyde & River Don Castings Ltd.*, 511 U.S. 202, 215 (1994) ("public policy wisely encourages settlements"); *Armstrong v. Board of Sch. Directors*, 616 F.2d 305, 312 (7th Cir. 1979) ("It is axiomatic that the federal courts look with great favor upon the voluntary resolution of litigation through settlement."). At the same time, settlements in derivative actions must avoid unfairness and collusion. *See, e.g., Birnbaum v. Birrell*, 17 F.R.D. 409, 411 (S.D.N.Y. 1955).

Rule 23.1 accommodates these competing concerns. On the one hand, it discourages unfair and collusive settlements by requiring prior notice to all shareholders, including nonparties, and by requiring prior judicial approval. On the other hand, it does not discourage settlement by imposing strenuous requirements, such as the unanimous consent of all shareholders or the successful appellate review of each proposed settlement. The procedural regime established by Rule 23.1 adequately protects the interests voiced by Petitioners without ignoring the competing interests at stake.

D. If Rule 23.1 Requires Amending, this Court Ought to Leave the Task to the Rulemaking Procedure that Congress Has Prescribed.

Even if every policy argument raised by CalPERS, SBA, and their *amici* were correct, this Court should still decline the invitation to amend Rule 23.1 through judicial legislation. Rule 23.1 does not contain words that can be fairly interpreted to include a right of appeal for nonparty shareholders who wish to appeal from

a district court's decision to approve the settlement of a derivative action. The only alternative is for the Court to rewrite the rules, which it has repeatedly—and rightly—refused to do.

Only last year, in *Amchem Products, Inc. v. Windsor*, 117 S. Ct. 2231 (1997), the Court addressed whether federal courts may certify a class under FRCP 23 if they consider a settlement "fair," even if the class does not meet the test outlined in Rule 23(a) and (b). The answer was a resounding "No."

> [C]ourts must be mindful that the rule as now composed sets the requirements they are bound to enforce. Federal Rules take effect after an extensive deliberative process involving many reviewers: a Rules Advisory Committee, public commenters, the Judicial Conference, this Court, the Congress. . . . The text of a rule thus proposed and reviewed limits judicial inventiveness. *Courts are not free to amend a rule outside the process Congress ordered . . . .*

Amchem Products, Inc. v. Windsor, 117 S. Ct. 2231, 2248 (1997) (citations omitted) (emphasis added); *see also Omni Capital Int'l v. Rudolf Wolff & Co.*, 484 U.S. 97, 111 (1987) ("It is not for the federal courts, however, to create such a rule as a matter of common law. That responsibility, in our view, better rests with those who propose the Federal Rules of Civil Procedure and with Congress").

Amendment, when necessary, has been left open by the rulemaking process prescribed by Congress. *See* 28 U.S.C. § 2072 (1998). And that avenue has been regularly put to use. The Federal Rules of Civil Procedure were adopted or amended 64 times between

1962 and 1993. Order, 507 U.S. 1091, 1092 (1993). There is no need for the Court to invent a right of appeal where Rule 23.1 is silent. If necessary, Rule 23.1 can be amended again, properly—through the procedure ordained by Congress.

CONCLUSION

The judgment of the court of appeals should be affirmed.

Respectfully submitted,

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